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UNITED STATES-JAPAN TRADE

HEARING

BEFORE THE

SUBCOMMITTEE ON INTERNATIONAL TRADE

OF THE

COMMITTEE ON FINANCE
UNITED STATES SENATE

NINETY-NINTH CONGRESS

FIRST SESSION

MARCH 8, 1985

Printed for the use of the Committee on Finance

U.S. GOVERNMENT PRINTING OFFICE

45-934 O WASHINGTON : 1985

S361-54

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UNITED STATES-JAPAN TRADE

FRIDAY, MARCH 8, 1985

U.S. SENATE,
COMMITTEE ON FINANCE,
SUBCOMMITTEE ON INTERNATIONAL TRADE,
Washington, DC.

The committee met, pursuant to notice, at 11:04 a.m., in room SD-215, Dirksen Senate Office Building, Hon. John C. Danforth (chairman) presiding.

Present: Senators Danforth, Chafee, Heinz, Grassley, Long, Bentsen, Matsunaga, and Bradley.

Also present: Leonard Santos, staff member.

[The press release announcing the hearing and the statements of Senators Grassley and Bentsen follow:]

[Press Release No. 85-001, March 1, 1985]

COMMITTEE ON FINANCE SUBCOMMITTEE ON INTERNATIONAL TRADE SCHEDULES HEARING ON UNITED STATES-JAPAN TRADE RESOLUTION ISSUE

Senator Robert Packwood (R-Oregon), Chairman of the Committee on Finance, announced today the scheduling of a March 8, 1985, Subcommittee on International Trade hearing on United States-Japan trade.

The hearing will review Senate Concurrent Resolution 15, offered by Senator John C. Danforth (R-Missouri) and 36 other members of the Senate. Senator Danforth, Chairman of the Subcommittee on International Trade, will chair the March 8 hearing.

Senator Danforth said his resolution calls for increased United States access to the Japanese market and for a more equitable trading relationship between the two nations.

Senator Danforth noted the U.S. merchandise trade deficit with Japan reached the unprecedented level of $37 billion in 1984, accounting for almost one-third of the entire U.S. deficit with the world. He said the deficit was accumulated despite substantial growth in the Japanese economy, while American manufactured goods, forest products, key agricultural commodities and certain services where the U.S. has a comparative advantage failed to receive equitable access to the Japanese market.

Senator Danforth's resolution seeks continuation of Japanese restraints on automobile exports to the U.S., until U.S. exports to Japan are substantially increased and the bilateral trade deficit is reduced.

The hearing will begin at 11 a.m., Friday, March 8, 1985, in Room SD-215 of the Dirksen Senate Office Building.

PREPARED STATEMENT OF SENATOR CHUCK GRASSLEY

MR. CHAIRMAN: On July 5, 1984, I read an article in the Wall Street Journal entitled, "World Trade Pulling Out of Doldrums". I would, if I may, like to quote one small section of that article. It starts out as follows, "Trade is improving," asserts Arthur Dunkel, Director General of the General Agreement of Tariffs and Trade . . . however, he states, "I'm not sure that trade policy has begun to improve yet".

I would have to agree with Mr. Dunkel's assertions. In fact, I see the most pressing short-run challenge we have is to get the trading nations to return to existing international rules and stop trying to make runs around the system. The next challenge is to shore up the present system, by bolstering existing rules and hammering out new regulations for those sectors still not covered, such as services, investment and high technology.

Although I realize this hearing is to address the VRA's with Japan on Auto Imports and trying to open up our export market to Japan, our problems in trade go beyond the negotiations stage on product lines alone. We have seen Japan not only close the U.S. out of its market, but the Europeans and the Asian countries as well. This policy has further exacerbated our trade problems by having those Asian countries which cannot export into Japan divert those exports in to the U.S. market. That is a poor policy for Tokyo and more important from an international prospective, the United States . . . and Europe are being short sighted if we think Tokyo's favoritism in any one special category in and of itself helps us. In fact, the United States and Europe become dumping grounds for Asian goods that cannot get into Japan.

While I have never promoted a protectionist attitude before and it is not my intent to do so now. . . . I just want to state for the record that with the massive trade deficit Japan has accumulated with not only the United States, but other countries as well, unless they begin to open up their markets to all of our trading partners, we should give serious consideration to building an alliance with Japan's Asian trading partners and Europe to try to ensure that Japan's markets are open to all. This may have a greater impact than us lashing back unilaterally at Japan.

PREPARED STATEMENT OF HON. LLOYD M. BENTSEN

MR. CHAIRMAN: the purpose of this hearing, like many other similar hearings, is to bluster enough that our faithful trade negotiators can get the Japanese to open their door a crack to some of our trade. I suggest this strategy is not working. America should stop blustering and tell the Japanese what it has to have as a global power.

[From the Washington Post, March 6, 1985]

THE JAPANESE ILLUSION

(By Robert J. Samuelson)

The dispiriting ritual of American-Japanese trade negotiations was played out again last week. Americans complained about Japanese foot-dragging; the Japanese protested. This time it was about telecommunications equipment and plywood; before it has been about cigarettes, beef and satellites. I have a suggestion: Let's halt all trade negotiations with Japan. The Japanese need to open their markets in their own interests and, if they don't see that, I doubt we can persuade them otherwise.

The great Japanese illusion is that huge export surplus is a sign of strength. Japan's export obsession is understandable; about three-quarters of Japan's imports are fuel, food and raw materials, so it needs to export to survive. But the obsession is backfiring. Since 1979, fully 40 percent of Japan's economic growth has stemmed from exports. This rising dependence on exports for growth and jobs makes Japan an easy prey for protectionism here and elsewhere.

Don't mistake me. I'm not advocating protectionism. At best, it's a short-term expedient that hurts American consumers. Import limits on automobiles raised car prices nearly 8 percent in 1984 while saving only 44,000 American jobs, according to a recent government estimate. At worst, protectionism invites imitation and retaliation, threatening the global trading system on which most nations, and Japan particularly, rely. But Japan abets protectionism by its own exclusionary practices.

Japan often doesn't buy even when foreign firms are clearly competitive. In 1984, the United States—which has the world's best communications system—ran at least a $900 million trade deficit with Japan in communications equipment. Little wonder, then, that a lengthening list of industries now has a potential stake in restrictions on Japanese imports. A decade ago, the list would have included steel textiles and televisions. Now you can add autos, auto parts, machine tools, telecommunications, electronic semiconductors and earth-moving equipment.

In short, the conditions are being laid for a protectionist binge; not now, but at the next economic downturn. In today's economy, most industries (surely telephones, even autos) are doing well. Witness the president's decision last week not to ask for a renewal of auto-import limits. But in a slump, when profits plunge and jobs disappear, protectionist pressures tend to overwhelm the diffuse interests of consumers or the abstract virtues of open trade. The best antiprotectionist defense is a large American lobby that has a stake in doing business with Japan, but this is precisely what's missing.

Americans (and others) don't feel they have a fair shot at the Japanese market, and for this Japan has only itself to blame. It is efficient at importing only what it absolutely needs—foods, fuel, minerals. In 1981, six major trading companies accounted for more than half of Japan's imports. But elsewhere, importers collide with cumbersome bureaucracy, parochial testing requirements, exclusionary trade associations or, simply, a predisposition not to buy foreign.

Consider telecommunications. Until recently, the state-owned telephone monopoly, NTT, purchased virtually nothing abroad. Now NTT is losing its monopoly, and Japanese government is considering new technical rules for approving foreign-made equipment. "What I hear makes me sweat at night," said Wolfgang Schwarz, vice president at Rolm Corp., a manufacturer of advanced switchboards and terminals. The new requirements may be "more complex and more cumbersome than the existing ones," he said.

The informal protectionism is typical. Japan's average tariff is lower than ours and formal quotas are few. But the Japanese government doesn't want to buy foreign satellites; a state monopoly and high tariff have restricted the sale of foreign cigarettes; tariffs of up to 20 percent remain on plywood imports; and quotas still restrict beef and citrus sales. The result is what economists call a low "elasticity" to imports. As Japan's economy grows, the demand for added imports increases only slowly. Japan's elasticity is less than half that of most other industrial nations.

Because much of the rest of the world buys Japanese, this is an inherently explosive situation. Nor is it automatically self-correcting. Much of Japan's export surplus is being invested abroad in dollar securities. Therefore, the surplus isn't leading to an appreciation of the yen (which would dampen the export boom) or to higher domestic spending (which would provide some stimulus to imports). Japan's domestic economic performance has been spotty; since 1979, exports have increased from 16 to 22 percent of gross national product.

Not only is this export-led growth a drag on the global economy, but it's a dangerous dependence for a nation that is perceived abroad as selfish. The United States and Japan have huge mutual interests and, as the world's two most technologically advanced nations, have a lot to teach each other. But these mutual interests are vulnerable to an uncontrollable spasm of protectionism. The truth is that no one really needs Japanese imports. Almost everything they export is (or can be) made elsewhere.

I am not saying that we ought to demand a balance in our trade with Japan. The whole point of trade is to shop around the world for the best available products. Nor did the Japanese single-handedly cause last year's huge bilateral imbalance, which was $34 billion in Japan's favor. Much of that stemmed from high economic growth here (which increased imports) and the high dollar (which made American exports less competitive). But foreign firms—not only American ones—that have a natural market in Japan need to realize that market; otherwise, the basic political requirement for trade, a sense of mutal advantage, vanishes.

Japan's interests are to fortify the international trading system; to export, it must import. I don't think American government officials can change Japanese attitudes or policies through negotiations. A decade of trying has yielded—as measured by imports—only meager results. The process of reaching agreements has substituted for the genuine goal of opening markets. So call the negotiators home. Great nations do not negotiate so much as they initiate. Japan is a great nation. It should begin acting like one.

I think we have to face the fact that Japan does not want to import anything it already makes. That is a shortsighted policy, and it is bad economics, but it is their current policy. No sense crying about it. The question is, can we live with that policy? For "live with it" we will, if we continue to follow the policies of the last few years.

The best we can hope for, according to Secretary Baldrige, is that the Japanese would buy $12 billion more from us per year, using this strategy. And if past experi-

ence is any guide, we will get about 10 percent of what we ask for, or $1.2 billion. Is that what serves the national interest?

Let me lay out what I see as the major strategic considerations here.

First, continuing current policies means that Japan gets to export more than just cars and video tape recorders. They are exporting adjustment problems. Instead of their rice farmers, and leather workers, and aluminum and wood and paper and dozens of other workers having to find new jobs this year, our workers have to find the new jobs. We have to stand the cost of retraining, unemployment insurance, crime and dislocation that Japan will not stand as a result of imports. That is the first impact of Japanese protectionism on our strategic interests.

Second, Japan is a bad example.

The developing world—and particularly the newly industrialized countries such as Brazil, Mexico, Korea, and a dozen others—do not look at Japan as the industrialized West. They look at Japan as the first successful developing country. And they want to imitate the success.

That means every planning minister from Kuala Lumpur to Brasilia thinks that the way to economic success is the same kind of protectionism as Japan has. The Japanese model is spreading like wildfire in the developing world. That works against our interest, because developing countries used to be 40 percent of our exports. A new study I have had done for the Senate Democratic Working Group on Trade Policy shows this market is dropping as a share of our exports. It was 28 percent in 1981, then down to 26.5 percent in 1983. If the Third World becomes as protectionist as the Japanese, we are the losers.

The third effect of Japanese protectionism on our strategic interests is that they buy even less from the developing world than they buy from us. Recent statistics used by Ambassador Bill Brock are that the United States imports almost 60 percent of developing world exports. Europe imports about 30 percent. Japan imports 8 percent.

That means we have to import more from LDC's like Brazil and Mexico in order to help those countries pay off their debts than if Japan were importing its fair share. Japan is no help at all. That hurts our strategic interests because our people take the brunt of adjusting to the exports of the developing world, as well as to the exports of Japan.

Mr. Chairman, how will it change this situation if Japan now buys 10 percent of what Secretary Baldrige hopes to sell there? Of course, anything will help. And the four sectors the President is pushing are important. But I submit the current strategy does not help with any of the basic problems I have just described. Even if Mike Smith is splendidly successful in the current negotiations, we will still be making—or trying to make—very difficult adjustments to both Japanese and LDC exports, and Japan will still be in effect cutting off our export markets in both Japan and the developing world.

Was the cigarette machine negotiation a "success" in strategic terms? Or baseball bats? Or even the beef and citrus exercise last year? In each case we got a few dollars more exports, but our basic problems continue. The current "negotiation"—if you can call it that—will fail because our Government has not defined the right problem.

These repeated failures will eventually mean we get protection. Why? Because eventually, the pressure from Japanese export and the difficulties of adjustment here will be so great that the Administration will simply be forced to close large chunks of our market. That will just make us all poorer.

Fred Bergsten has already observed that this Administration has imposed more protection than any American Administration since the 1920's. And you remember that group: They brought us the Great Depression.

Now, what are the strategic answers? I do not know all the answers, but I do know we have to ask the right questions. I suspect much of the answer is to convince the President to do something about the budget deficit.

Part of the answer will probably have to be to prevent Japanese exports to this country until they open up their market to the world as a whole. But exact strategies should await an evaluation of our real interests.

Mr. Chairman, you joined with me last year in giving the Administration a roadmap that shows how to get out of this kind of dead end. Section 181 of the 1984 Trade Act directed the President to submit to us a National Trade Estimate, showing our major trade problems and the attacks he proposed to make on them.

The Senate Democratic Working Group on Trade Policy is going to work on this problem this year and report to the Democratic Conference on new approaches to trade policy that serve the national interest.

I hope, Mr. Chairman, you and I can work together again to tell the nation what its real trade dilemma is. Let's end the bluster and get down to business.

Senator DANFORTH. This is a hearing on the resolution that was introduced by Senator Boren and I, Senate Concurrent Resolution 15, dealing specifically with the question of extension of voluntary restraints on automobiles, but taking the position that the restraints should only be lifted when the United States has a fair access to the Japanese markets for the products that we want to sell to Japan. Therefore, the hearing is really not so much on the question of automobiles but on the question of the access that we have to the Japanese market. I have five propositions which I would like to state and which I think are deserving of consideration.

I believe each of these statements to be true, and I will state them.

Proposition 1: Trade problems that the United States experiences with Japan are not limited to the United States. That is to say that what we experience with Japan is something which is largely shared by the rest of the world. It is a global problem. It is a problem that is experienced not only by the United States but by Europe, by the lesser developed countries, by many others in the world. Japan has become a trade problem to the whole world.

Proposition 2: We have spent a lot of time recently talking about the value of the dollar, the relative value of the dollar compared to other currencies, especially to the yen. Proposition 2 is that trade deficits between the United States and Japan would exist probably at about the present level, although that is hard to know, with or without the exchange rate problem, that other countries have experienced trade problems with Japan even though the yen has been relatively highly valued compared to the currencies of the other countries.

Proposition No. 3: In the past 4 years or so, we have continued a long history of negotiations with Japan. We have sent many delegations to Japan, and we have received many delegations from Japan, and those negotiations have been a waste of time.

Proposition No. 4 is that the administration's policy of constant negotiations, while at the same time continually expanding Japanese access to the U.S. markets, regardless of the size of the trade deficit with Japan, and regardless of Japanese protectionism, is the wrong policy.

And proposition No. 5 is that the time has come to act, to do something—not to lose our tempers, not to make speeches. The old saying is: "Don't get mad, get even." The time has come to do something, take some specific action in retaliation for Japanese trade practices. Those are the five propositions that I would put before the committee and before the Senate. Senator Bentsen?

Senator BENTSEN. Thank you very much, Mr. Chairman. The purpose of this hearing, it seems to me, is like a lot of other similar hearings, and that is that we bluster and bluster to try to get the Japanese to open the door just a crack wider for some of our trade, and I suggest that strategy just isn't working. America ought to stop blustering to the Japanese and tell the Japanese what they have to do if they are really going to be a global power. I read this morning an article by Robert Samuelson, the economist. The arti-

cle is entitled, "The Japanese Illusion." He says, "I have a suggestion. Let's halt all trade negotiations with Japan."

The Japanese need to open their markets in their own interests, and if they don't see that, I doubt that we can persuade them otherwise. The great Japanese illusion is that a large trade surplus is a strength, and yet in the long run it will hurt them and hurt them badly.

I think we have to face the fact that the Japanese don't want to import anything that they already make. That is a shortsighted policy, and it is bad economics. That is their current policy. So, there is no sense crying about it. The question is: Can we live with that policy? For live with it we will if we continue the policies of the last few years.

The best we can hope for according to Secretary Baldrige is that the Japanese would buy $12 billion more from us per year using this strategy, but if the past experience is any kind of a guide at all, we will get about 10 percent of what we ask for, and that is $1.2 billion.

Is that what serves the national interest? Let me lay out what I see as some of the major considerations. First, continuing current policies means that Japan gets to export more than just cars and video tape recorders. They are exporting adjustment problems. Instead of their rice farmers and leather workers and aluminum and wood and paper and dozens of other workers having to find new jobs this year, our workers have to find the new jobs. They have to stand the cost of retraining, unemployment insurance, crime, and dislocation that Japan will not stand as a result of imports.

Now, that is the first impact of the Japanese protectionism on our strategic interests.

Second, I think Japan is a bad example, and a bad example in particular for the developing world, and particularly the newly industrialized countries, such as Brazil, Mexico, Korea, and dozens of others. They don't look on Japan as the industrialized West. They look at Japan as the first successful developing country, and they really want to imitate that kind of success. That means every planning minister Kuala Lumpur to Brazilia thinks that the way to economic success is the same kind of protectionism that Japan has, and the Japan model is spreading like wildfire throughout the developing world. That works against our interests because developing countries used to take up to 40 percent of our exports. A new study that I have had done for the Democratic working group on trade policy shows that this market is dropping as a share of our exports. It was 28 percent in 1981 and down to 26 percent in 1983. Now, if the Third World becomes as protectionist as the Japanese, we are the losers.

The third effect of Japanese protectionism on our strategic interests is that they buy even less from the developing world than they buy from us. Recent statistics used by Ambassador Bill Brock show that the United States imports almost 60 percent of developing world exports—almost 60 percent. Europe imports about 30 percent, and the Japanese import about 8 percent. Now, that means we have to import more from LDC's like Brazil and Mexico in order to help those countries pay off their debts, than if Japan were importing their fair share. The International Monetary Fund

in a sense encourages this by saying to all of these countries—the developing countries if they are in trouble—look, you have to cut back on your imports, and you have to increase your exports.

Who is absorbing the increase? Most of it is coming here to the United States. Now, that is where we need some help from the Japanese. Mr. Chairman, how would it change this situation if Japan were to buy 10 percent of what Secretary Baldrige hopes to sell there? Of course, it is going to help, but I submit the current strategy doesn't help with any of the basic problems I have just described. Even if Mike Smith is splendidly successful in the current negotiations, we will still be making or trying to make very difficult adjustments to both Japanese and LDC exports, and Japan will still be in effect cutting off our export markets in both Japan and the developing world.

Mr. Chairman, we have others that want to make their statements, I'm sure, and I have a rather lengthy one, but I will put the rest of it in the record.

Senator DANFORTH. All right. Thank you very much, Senator Bentsen.

Senator BENTSEN. Thank you, Mr. Chairman.

Senator DANFORTH. Senator Grassley.

Senator GRASSLEY. Thank you, Mr. Chairman. I would like to put a statement in the record. In addition to that statement, I would like to thank Senator Danforth, the chairman of the committee; Senator Boren, and all who have cosponsored this resolution, basing the termination of Japanese restraints on all exports to the United States, on the increased exports to Japan, and a reduction of the U.S. trade deficit. I think that the President has a real opportunity to express some quid pro quo's from the position that he wasn't going to ask for the imposition of the voluntary restraints again. And I think that when we do that, as a nation, we are not further supporting the perception of the United States as being a paper tiger in international trade.

We say we expect things, that we believe in free trade, and yet we allow our trading partners to confront us by taking away a large share of our markets by either closing their doors to our products coming into their countries or through subsidies. And we have lost a good share of the world market just because we have taken the attitude that we are a great big, strong nation. Somehow we think we don't really have to worry about our share of international trade, because people are going to be running to America for our products like they did during the 1950's and 1960's.

It is a whole new ball game now in international trade. Unless we as a government take a strong position and support that position with the fact that we have a deep pocket, and we are going to use that deep pocket until we either get free trade, or else abandon it entirely, we are going to continue to lose market shares.

And I commend the leadership of this committee for taking the attitude of quid pro quo on various issues that are up for negotiation. Now we need to have the President take a much stronger position in order for the United States to achieve any progress in the negotiations. And I mean real progress, not the kind where we just sit down and talk, as opposed to negotiate, and where we think we get victories, and later find out that what we thought was progress

was nothing. I know there is a little bit of progress here and a little bit of progress there, but in reality it doesn't turn out to be what we read about in the papers and what we think and what our people come back and think they got—whether it be private sector people or whether it be our Government officials.

I think it has reached a point where enough is enough. If our so-called friends don't want to continue to work with us, then instead of the cooperation we have enjoyed for the last 30 or 40 years, we will have confrontation, and the confrontation is going to become more vigorous and more economically retaliatory. Getting to where we have to go means simply this: that free trade means free trade and that we have got to have progress made in getting this trade deficit down.

Senator DANFORTH. Senator Bradley.

Senator BRADLEY. No opening statement.

Senator DANFORTH. Senator Chafee.

Senator CHAFEE. Thank you, Mr. Chairman. Mr. Chairman, I come at this from a somewhat different viewpoint than many here. I don't quarrel with the trade deficit that we have with Japan. I don't think that is the question or indeed the problem. Frankly, if you look at the statistics, you will see that our exports to Japan indeed have been growing over the past several years, not growing as much as their exports to us, but they have been growing. And frankly, in areas of the world where we traditionally have had trade surpluses, say the European Community—for years and years we ran trade surpluses—but we have had no congressional investigation of that. The real problem is not the imbalance. The real problem is the accessibility of the Japanese markets to our products which are acknowledged to be superior to their manufactured products.

Now, for example, in the automobile business, I approve of the lifting of the voluntary auto restraints. I think that was right. I think there is little suggestion that American automobiles would sell in Japan in any substantial quantities. There is acceptance by the American population, by American consumers of the Japanese automobiles. They look on those Japanese automobiles as better automobiles in many instances, at least they show it with their pocketbooks—they prefer Japanese automobiles to those that they can buy here, and I am not quarreling with that. That is an advantage for the American consumer that we ought to continue. So, the trade imbalance isn't the point. The point is that there is denied accessibility to the Japanese markets for our products. We accept their products, and that is the way it should be. It is better for our consumers. At the same time they must admit our products into their markets, and that is something that they are not doing. Now, the thing we can focus on—there is a variety of products that we can deal with—foods and lumber—but it seems to me the most clear cut is the telecommunications industry and equipment.

Now, how do we get their attention? Mr. Olmer and others have made trip after trip to Japan. We have had high level visitations of all types, including the Prime Minister, Vice Presidents, Presidents, to deal with this matter, but nothing seems to happen except promises and studies and further consultations. The result is no progress, no substantial progress at all. And so, it seems to me, Mr.

Chairman, that indeed the American Congress representing the American people have reached a point of frustration, and I for one, who has been the most supportive I think of anyone on this committee of the accessibility of our markets to the Japanese products, have reached that point as well. Now, when we try to retaliate, it is always clumsy. It is not clean cut, but what else can we do? And Mr. Chairman, I think we have now reached a point where we have got to choose some form of retaliation. Maybe it is the form of denying all admittance to our markets of their telecommunications products or all their electronics products. That would get their attention pretty quickly. What I am saying, Mr. Chairman, is that we have now reached the point that we have got to do something and we have got to do something decisive in order to end this impasse that has continued for so many years. Thank you, Mr. Chairman.

Senator DANFORTH. Thank you. Senator Heinz?

Senator HEINZ. Mr. Chairman, thank you very much. I commend you on holding this hearing. It comes at a critical time, and I have listened to my colleagues and agree with virtually everything they have said, but having said that, I am not sure that we have identified the real core of the problem. Yes; John Chafee says, certainly part of it is accessibility to markets, but I would suggest, that there is something even more profound than just keeping us out of some markets with performance requirements and the like. I was struck by the very last paragraph in the article that began on the front page of today's Washington Post which says: "Japanese plead for patience on trade surplus." Of course, the trade surplus with Japan did not happen overnight. The Japanese had a $9 billion trade surplus in 1979. It doubled within 3 years, and it doubled again 3 years after that, coming up to the roughly $37 billion surplus that it is today. And hence, the quotation from Mr. Okita, a very sage and wise individual by the way, who I spent some time with this morning, is quite revealing. He said the figure is getting too large in a very short period. I don't think that is as accurate as the statistics I have cited. But he went on to say that sometimes political change can't catch up. And you know, I suspect that really is what we are talking about with respect to Japan because they have a policy of protecting their infant industries until they are big industries by keeping us and other people out too. They have a policy of industrial targeting, which means doing all the things that are necessary to help what they perceive to be the growth industries of the future, while keeping everybody out.

They have a process of adjustment with respect to, say, some very small industries that they have had for a long time which, when you suggest that maybe they should let a little bit more beef in from this country, they say, oh, you can't expect us to make rash decisions even though we are talking about a problem that has existed for 15 or 20 years. Their escape clause is not limited to 5 years as is ours—it is limitless. What is happening, however, is not that, in and of itself. What happens when you protect an infant industry and it becomes large is that a lot of politicians start protecting that industry. What happens when you start successfully targeting an industry is that as it becomes more successful, more politicians begin to support it. The same thing is true of the industires that have been around for a long time. The result, of course, is that

there is a huge political vested interest in Japan in the kinds of protectionism that we have all seen, that we have all described. And even the best intentioned people, such as Prime Minister Nakasone, Mr. Okita and others, may not even realize the depth of the political problem in Japan. That is why John Chafee and others are right, but there is probably an insoluble political problem reflected in the bureaucracy, and remember, their politicians are also in the executive branch as well as in the Diet.

The fact is that there is almost no alternative but a political decision taken by our political bodies—the executive branch and the Congress—as a reaction to their political stance, which is ingrained. By the way, protectionism is not new in Japan. It has its roots, at least in terms of the protection of infant industries, in the Meiji dynasty. The Japanese to this day remain very conscious of their vulnerability to imports, particularly energy and other raw materials. They have some good reasons in their national psyche to be concerned about it. The immediate efficient cause of their bombing Pearl Harbor was our cutting off of gasoline supplies to their military, and the decision of their military that it was better to fight the United States when they were strong rather than when they were weak. It is a very sore spot—an Achilles heel. And I cite that because the problem really runs deep within the Japanese culture and is externalized in the behavior of their politicians and the protectionist manifestations that we are all familiar with.

And so, it is my view, Mr. Chairman, that there is going to have to be a political solution. There is going to be a sudden, strong, and unpredictable political reaction to Japanese protectionism, and maybe we will take the course, as John Chafee has suggested, of simply shutting our market to Japanese electronics or telecommunications equipment or high tech or some other combination of goods and services to make the point. But I can tell you, unless we make the point politically, we will be going through this exercise forever because this headline that I started with—Japanese urge patience—is the same one that has been on the front page of our newspapers and business sections for each of the last 5 or 6 years. Please be patient. And meanwhile the trade deficit with Japan keeps going up. And by the way, it has nothing to do with the strong dollar. The strong dollar is a problem, but every other developed country—whether it is Japan's second largest trading partner, Korea, where the Korean currency is weak, vis-a-vis the yen, or others—has exactly the same problem that we do. The West Germans have the same problem. Their imports from Japan grow. Their exports don't, and the German mark is weak, vis-a-vis the yen, and has been for some time. So, what I am suggesting, Mr. Chairman, I suppose, is that there really is no alternative but for the politicians in this country to take note of the politicians in Japan and the kind of action that we must take in order to change the balance. I thank the Chair.

Senator DANFORTH. Thank you, Senator Heinz. Senator Long?

Senator LONG. No questions at this time.

Senator DANFORTH. Now, before we get to the two very distinguished witnesses we have, I have asked Leonard Santos of the Finance Committee staff if he would make a very brief factual pres-

entation so that we have the background of the present situation before we get to the panel.

Mr. SANTOS [pointing to charts]. Mr. Chairman, the first chart here lists the major market opening announcements of the Japanese Government and discussions between President Reagan's administration and the Japanese Government, starting in 1982 and running down to the most recent agreement on undersecretarial delegation discussions in Tokyo, which was agreed to at the meeting between President Reagan and Prime Minister Nakasone. This listing, of course, is just since 1982. These are the major events in that period. There have been many low level exchanges, and, of course, there were many exchanges prior to 1982 as well. This list is contained in the committee memo as well.

CHART I

January, 1982	• First trade package announced.
May, 1982	• Second trade package.
June - Nov 1982	• Several staff level trips to Tokyo to discuss implementation of these measures.
January, 1983	• Third trade package.
	• First Reagan/Nakasone Summit. Need for market access in Japan noted.
October, 1983	• Fourth trade package.
November, 1983	• President Reagan visits Toyko. Launches an intensive effort to address major bilateral trade issues. Vice President Bush coordinates for U.S.
January - April, 1984	• Followup negotiations.
January, 1984	• NTT Agreement renewed.
April 27, 1984	• Fifth trade package. Addresses several key issues.
May, 1984	• Vice President Bush visits Tokyo. Welcomes package but notes we have a long way to go.
	• "Yen-dollar accord" announced.
January, 1985	• Reagan/Nakasone Summit in California. The sectoral initiative launched.
January 28-29, 1985	• Undersecretarial delegation visits Toyko to begin sectoral negotiations.

CHART II

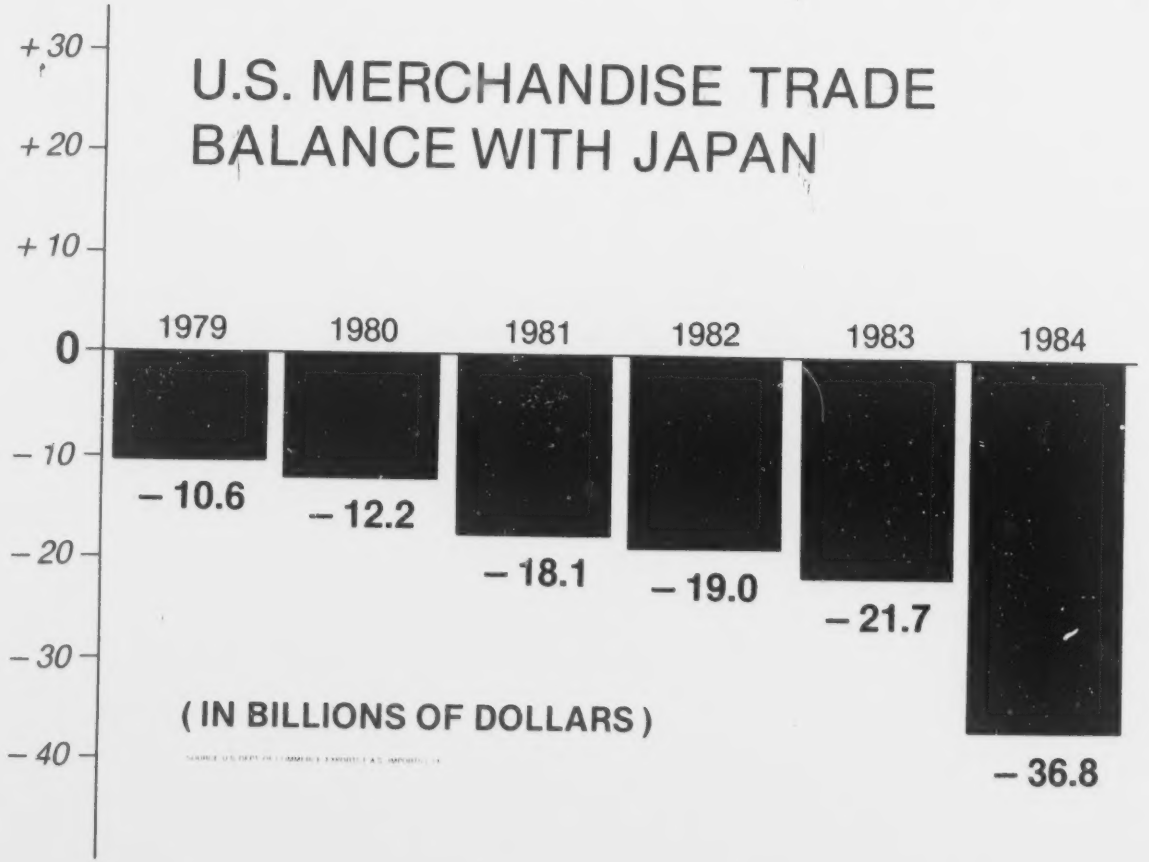
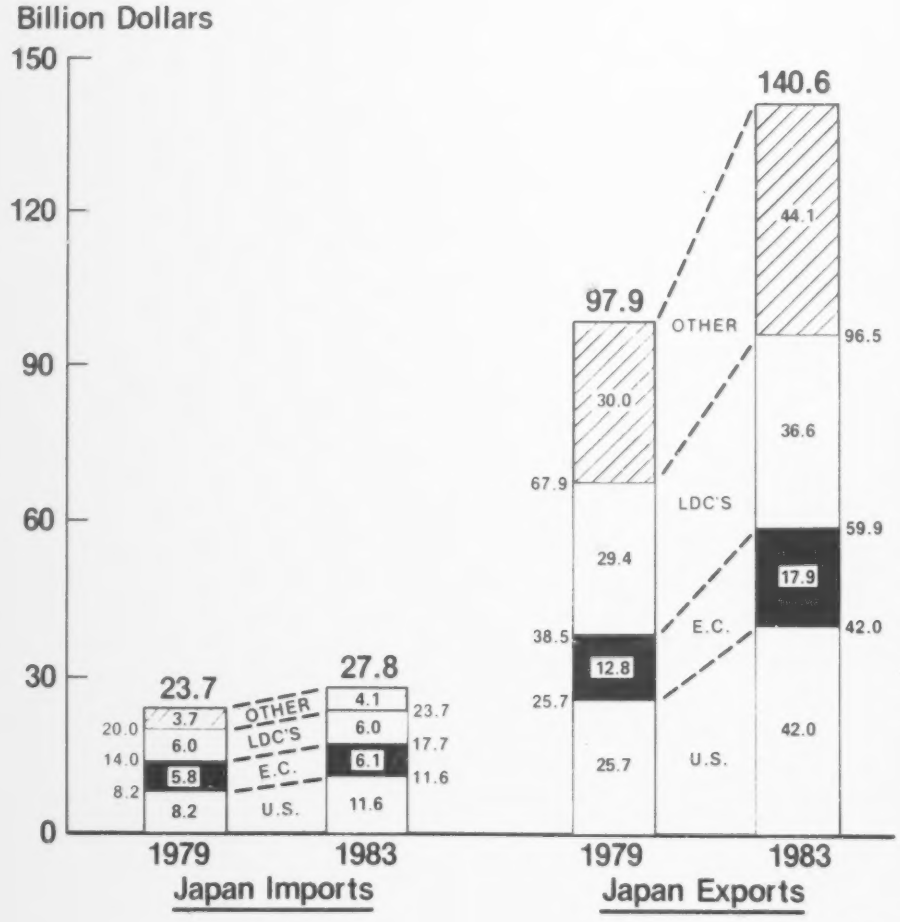

U.S. MERCHANDISE TRADE
BALANCE WITH JAPAN
+30
+20
+10
0
-10
-20
-30
-40
1979
1980
1981
1982
1983
1984
-10.6
-12.2
-18.1
-19.0
-21.7
-36.8
(IN BILLIONS OF DOLLARS)

CHART III

JAPANESE TRADE IN MANUFACTURED GOODS



Source: GATT

The next chart is a chart of the bilateral merchandise trade deficit. As several members of the committee have noted, that deficit has about doubled since 1982 and, in turn, it had about doubled since 1979. I should note that this is the merchandise trade balance. It is not the current account balance. The current account deficit would be almost as large as the merchandise trade deficit, which is unusual in bilateral trade balances. The current account generally is much smaller than the merchandise trade deficit.

Senator BRADLEY. Mr. Chairman, may we ask questions in the course of the presentation?

Senator DANFORTH. Sure.

Senator BRADLEY. What would be the deficit if you added the capital account balance?

Mr. SANTOS. For example, in 1983, I think the number for the current account was approximately minus $18 billion. So, in effect, the earnings—the return on capital reduced the bilateral deficit by $3 billion. The current account combines the merchandise trade deficit with the return on investments, service income, interest payments, et cetera. So, that return reduced the bilateral deficit by about $3 billion. That is unusually small. For example, right now with Canada, I believe, the merchandise trade deficit is about $20 billion, and yet the current account is almost in balance. The final chart is a chart of Japan's manufacture trade with the rest of the world. The blue section reflects their manufacture trade with the United States. The orange section reflects their bilateral trade with the European Community. The yellow section reflects their bilateral trade with the less developed countries and the final section reflects bilateral trade with the rest of the world, which would include Australia, Canada, and other countries.

As you will see, Japan's balance of manufactured trade is even more in surplus than is its overall trade, so that there is an even greater gap between Japan's exports and imports. That is not entirely surprising in view of the fact that Japan must export to purchase the raw materials that it does not have.

Senator DANFORTH. Tell us again what the colors are.

Mr. SANTOS. The blue colors are U.S. merchandise trade—manufactured trade balance. The orange colors are the balance for the European Community. The yellow colors are the balance for the less developed countries, and the top, lined orange, is the rest of the world.

Senator HEINZ. Mr. Chairman, I don't think the right term is balance. The two columns on the left are imports, and the others are, on the right, exports.

Mr. SANTOS. That is correct.

Senator HEINZ. And they don't—per se, there is no balancing.

Mr. SANTOS. The difference between these two numbers would be a balance in manufactured goods.

Senator HEINZ. Yes.

Mr. SANTOS. There are several things to note. Of course, there is a tremendous difference between Japan's imports of manufactured goods and its exports of manufactured goods. What is perhaps interesting to note is that Japan's imports of manufactured goods from the European Community, from the less developed countries, and from the rest of the world has hardly changed in the 4 years

from 1979 to 1983. Actually, the United States, compared with these other groups, has fared relatively better even though its exports to Japan have grown moderately. One of you mentioned that, for example, the less developed countries, which are forced to export to pay their debt obligations, are doing so to the United States. This figure reflects that Japan's absorption of developing country exports—manufactured exports—virtually has not changed over this period of time, and the EC has also experienced only a slight change. Worthy also to note is that many of the currencies of these countries—the German mark was mentioned, the French franc, the British pound, the Korean wan, et cetera—many of these currencies have, in fact, depreciated against the Japanese yen, and it has not apparently been reflected in Japanese imports of manufactured goods.

Senator BRADLEY. Mr. Chairman, could I just go back to this last point because I think it is very important to try to get the exact facts. You had a merchandise trade deficit on the previous chart of what—$21 billion?

Mr. SANTOS. In 1983, it was $21.7 billion.

Senator BRADLEY. Now, how much of the net capital outflows from Japan came to the United States to purchase U.S. Government securities, and other debt instruments?

Mr. SANTOS. I do not have that figure. It is, I believe, quite a large number. It would, however, not necessarily show up in the current account balance, which is not a measure of assets and liabilities. It is measure of the flows. I don't have the precise figure for Japanese exports of capital.

Senator BRADLEY. So, we don't know how much capital Japan put into the country to subsidize our deficit?

Mr. SANTOS. I don't have that figure. I believe it can be obtained, and if you want it included in the record, we can do so. It is a very large figure. They are a major exporter of capital.

Senator BRADLEY. Could we include that in the record?

Mr. SANTOS. Of course.

[Len Santos subsequently submitted the following statistics for the record:]

[In millions of dollars (capital inflow +; capital outflow −)]

1981	+9,298
1982	−1,992
1983	+7,225
1984	+13,504

NOTE.—There is considerable uncertainty in these numbers, and some private sector sources put net Japanese capital flows to the United States considerably higher.
Source: Department of Commerce, Bureau of Economic Analysis.

Senator DANFORTH. Any further questions?

Senator CHAFEE. Mr. Chairman, of course, manufactured goods are not all important, but it is interesting to note that the imbalance of Japan's exports versus imports are tenfold with other nations. They are sixfold with the LDC's. They are threefold with the European Community, and a little less than fourfold for the United States. So, whatever experience we have with manufactured goods is at least constant with what other nations or other sections of the world are experiencing, and indeed less—considerably less.

Senator DANFORTH. That is an excellent point—that misery loves company. The point is that this is a global problem. This is a problem not just that the United States has with Japan, but the world has with Japan. We worry about the debtor nations. We worry about the lesser developed countries—they are all in the same boat. Everybody is in the same boat. It is said that the problem is unique to the United States. We are not trying hard enough. It is not unique to the United States. It is said that the problem is the exchange rate, the value of the dollar. That is obviously a problem, but regardless of the exchange rate, countries that don't have the exchange rate problem have exactly the same difficulty. And when you compare those puny little columns on the left with those huge towers on the right and what has happened between 1979 and 1983, it is an amazing story, and that has not stopped in 1983, has it, Len?

Mr. SANTOS. The pattern has accelerated. Our imports of manufactured goods last year from Japan increased about 39 percent. Our exports of manufactured goods to Japan increased about 9 percent. So, the gap is, in fact, widening.

Senator DANFORTH. And how about the rest of the world?

Mr. SANTOS. It is clear that the gap has widened, not to the same extent as it has for the United States. The gap has accelerated more with the United States.

Senator DANFORTH. Thank you very much. Ambassador Smith?

STATEMENT OF HON. MICHAEL B. SMITH, DEPUTY U.S. TRADE REPRESENTATIVE, OFFICE OF THE U.S. TRADE REPRESENTATIVE

Ambassador SMITH. Thank you, Mr. Chairman. It is obviously a pleasure to be with you here today and to share with you and to discuss with you some of the efforts that we are undertaking now to see if we can improve our access into the Japanese market. As you know, sir, we have been engaged in a very intensive trade dialog with Japan, particularly over the past 6 weeks, and we have had delegations led by Under Secretary Wallace, Under Secretary Olmer, Under Secretary Amstutz of the Department of Agriculture, and me, to meet with the Japanese in ways that we could negotiate improvements in market access. This undertaking was set in motion by a commitment that the President received from Prime Minister Nakasone during their meeting in Los Angeles in early January. Four sectors were identified for negotiation with the expectation, and we believe understanding, that other additional sectors would follow. For the moment, however, our attention is focused on telecommunications, which Lionel Olmer will speak about in a moment, electronics, forest products, and medical equipment and pharmaceuticals. This process that we have undertaken, sir, is different than previous negotiations, as these discussions are intended to address all the barriers in each sector. We want to remove every obstacle to trade across entire sectors, and not to be drawn into a peeling-the-onion approach in which the removal of one barrier simply reveals another underlying layer of protection.

Our goal is obviously a fundamental transformation in the degree of openness of the Japanese market. We are looking for con-

crete results, measurable by increased sales, by market shares for farm products, or by indications in the business community that indeed we have made substantial progress. Every one of the teams of the four sectors is led by an Under Secretary to ensure continual high level and political commitment. Obviously, the President, Secretary of State, Ambassador Brock, Secretary Baldrige, and Secretary Block will follow the progress of these negotiations and we will review them with Prime Minister Nakasone and appropriate members of his cabinet during the coming months. There is no final cutoff date to these discussions, sir, but certain check points suggest themselves. In the telecommunications sector, for example, April 1. By that date, we hope and we presume that we will have a reasonable fix on the ground rules under which U.S. suppliers of telecommunications services and equipment will be able to compete with Japan. The Bonn Summit in May offers another opportunity for the President and the Prime Minister to review the progress made in all the sectorial discussions, and there will be meetings between April 1 and the time of the summit with various cabinet officers to serve also as check points. I will pass over telecommunications in the interest of time, sir, since Lionel will be spending a great deal of time on that.

I would like to turn if I could to forest products. As you know, Under Secretary Amstutz of the Department of Agriculture, held a meeting on forest products in Tokyo on February 25. In that session he explained our view and the view of our forest products industries that tariffs are the most important obstacle we now face in this sector. The Japanese side refused to consider the possibility of tariff changes at this time, a position which we consider inconsistent with the mutual understanding on which these negotiations are based. We are now considering steps to move the work of this team ahead.

On electronics, sir, we have had one meeting with the Japanese, again in Tokyo, on this sector. Many of the problems in this sector are familiar to us from earlier discussions, as for example, in the United States-Japan high technology work group. In the past, I think we have had some success in this area, as in the mutual elimination of semiconductor tariffs. We will meet again on March 18, and our agenda for these discussions is, has been, and is being developed in close consultation with American private industry.

On medical equipment and pharmaceuticals, we will meet in Tokyo next week for our first meeting to discuss this sector. A good deal of preliminary work has been done in this area over the past few years, particularly on problems related to standards and certification, acceptance of clinical test data, and regulatory issues. We have been meeting here in Washington with private industry representatives as well as talking with the U.S. firms that are represented in Tokyo to get a clearer understanding of how this sector operates in Japan. We need to understand in this regard how the problems our companies face each step along the way—that is to say, at the border, in product approval, in manufacturing and in distribution—all fit into the sector as a whole. In this way, we hope to avoid the pitfall of getting mired down in a specific problem area and losing sight of the broader goal of opening up this entire sector. In addition to these four sectors that are the subject of this

concerted attention, sir, there are of course the ongoing negotiations in other trade areas.

Next week, for example, I will chair a meeting of the United States-Japan Trade Committee in which we will pursue a broad range of market access issues, including tariffs, services, tobacco, GATT disputes, and standards issues, among other matters.

We will repeat our request for tariff cuts on a wide range of items, including aluminum, chocolate confectionery, fresh grapefruit and walnuts, photographic film, aramid fibers and wine. We will talk about lawyers and we will finish our discussions on the privatization of Japan's tobacco and salt monopoly, an area in which we have worked very closely with our tobacco products exporters.

As you can see, sir, our present trade dialog with Japan spans nearly the whole range of our trade relationship. The focus of that dialog including the high level sectoral discussions set in motion by the President and the Prime Minister, as well as our talks in the Trade Committee and other trade fora, is market access. Our goal remains an across-the-board reduction in the barriers that our exporters face in Japan, so that the opportunities that U.S. companies have to sell in Japan are comparable to those that Japanese companies have here in the United States.

This kind of openly competitive environment would benefit consumers in our two countries and, provide the stimulus needed by industries in both countries and with specific reference, sir, to one other point that you and Senator Bentsen made, would show an example so that the other countries of this world do not make the mistake of slipping further into protectionism. Thank you, sir.

[Ambassador Smith's prepared statement follows:]

OFFICE OF THE UNITED STATES
TRADE REPRESENTATIVE
EXECUTIVE OFFICE OF THE PRESIDENT
WASHINGTON
20506

STATEMENT OF

AMBASSADOR MICHAEL B. SMITH

BEFORE THE

SUBCOMMITTEE ON INTERNATIONAL TRADE

OF THE

SENATE FINANCE COMMITTEE

MARCH 8, 1985

MR. CHAIRMAN:

IT IS A PLEASURE TO BE WITH YOU TODAY TO DISCUSS SENATE CONCURRENT RESOLUTION 15, WHICH YOU AND SENATOR BOREN INTRODUCED ON FEBRUARY 20. AS YOU KNOW, WE IN THE OFFICE OF THE UNITED STATES TRADE REPRESENTATIVE WELCOME THE ATTENTION WHICH THIS COMMITTEE GIVES TO OUR TRADE RELATIONSHIP WITH JAPAN. WE SHARE YOUR CONVICTION THAT ACCESS TO JAPAN'S MARKETS MUST IMPROVE, AND I WELCOME THIS OPPORTUNITY TO DISCUSS WITH YOU THE EFFORTS WE HAVE UNDERWAY TO ACHIEVE THAT GOAL.

<u>TERMINATION OF JAPAN'S VOLUNTARY RESTRAINT ON AUTO EXPORTS</u>

BEARING IN MIND THIS COMMITTEE'S INTEREST IN JAPAN'S VOLUNTARY RESTRAINT ON AUTOS, AND THE CONCERN EXPRESSED IN THE RESOLUTION WHICH YOU AND SENATOR BOREN HAVE CO-SPONSORED, I WILL BEGIN

MY REMARKS WITH A COMMENT ON THE PRESIDENT'S DECISION NOT TO URGE CONTINUATION OF THAT RESTRAINT. THAT DECISION WAS TAKEN IN LIGHT OF THE RETURN TO HEALTH OF THE AUTO INDUSTRY, WHICH EARNED RECORD PROFITS OF $9.8 BILLION IN 1984. IT WAS TAKEN IN VIEW OF THE SHARP IMPROVEMENT IN AUTO INDUSTRY EMPLOYMENT, WHICH EXCEEDED 900,000 WORKERS THIS JANUARY, AN INCREASE OF 200,000 WORKERS SINCE 1982. FURTHERMORE, THE DECISION REFLECTS A DETERMINATION TO LIFT THE BURDEN THAT THE RESTRAINT IMPOSED ON CONSUMERS. THE VOLUNTARY RESTRAINT IS ESTIMATED TO HAVE COST U.S. CAR BUYERS NEARLY $16 BILLION OVER THE PAST FOUR YEARS.

IN SUM, THE RECOVERY OF THE AUTO INDUSTRY, THE COST OF THE RESTRAINTS TO CONSUMERS, AND THE CONVICTION THAT OUR ECONOMY IS MOST PRODUCTIVE WHEN IT MUST RESPOND TO COMPETITIVE FORCES, BROUGHT THE PRESIDENT TO THE CONCLUSION THAT JAPAN'S RESTRICTION OF AUTO EXPORTS IS NO LONGER IN THE INTEREST OF THE UNITED STATES.

THIS ACTION DEMONSTRATES THAT WE BELIEVE OUR INTERESTS ARE BEST SERVED BY FREE TRADE. JAPAN SHOULD SEE THE DECISION AS AN INDICATION THAT IT MUST TAKE ACTION TO OPEN ITS OWN MARKETS TO COMPETITION FROM U.S. EXPORTS.

U.S. - JAPAN TRADE NEGOTIATIONS

WE ARE NOW ENGAGED IN AN INTENSIVE TRADE DIALOGUE WITH JAPAN. DURING THE PAST 6 WEEKS TEAMS LED BY UNDERSECRETARY OF STATE

WALLIS, UNDERSECRETARY OLMER, UNDERSECRETARY AMSTUTZ OF THE DEPARTMENT OF AGRICULTURE AND ME HAVE MET WITH THE JAPANESE TO NEGOTIATE IMPROVEMENTS IN MARKET ACCESS. OUR WORK WAS SET IN MOTION BY A COMMITMENT THE PRESIDENT RECEIVED FROM PRIME MINISTER NAKASONE. IN THEIR MEETING JANUARY SECOND IN LOS ANGELES, THE PRIME MINISTER PLEDGED TO WORK WITH US TO REMOVE BARRIERS TO TRADE IN JAPAN. FOUR SECTORS WERE IDENTIFIED FOR NEGOTIATION, WITH THE EXPECTATION THAT ADDITIONAL SECTORS WILL FOLLOW. FOR THE MOMENT, OUR ATTENTION IS FOCUSED ON TELECOMMUNICATIONS, ELECTRONICS, FOREST PRODUCTS, AND MEDICAL EQUIPMENT AND PHARMA CEUTICALS.

THE PROCESS WE HAVE BEGUN IS DIFFERENT FROM PREVIOUS NEGOTIATIONS. THESE DISCUSSIONS WILL ADDRESS ALL BARRIERS IN EACH SECTOR. WE INTEND TO WORK WITH JAPAN TO REMOVE EVERY OBSTACLE TO TRADE ACROSS ENTIRE SECTORS, NOT TO BE DRAWN INTO A "PEELING THE ONION" APPROACH, IN WHICH REMOVAL OF ONE BARRIER SIMPLY REVEALS ANOTHER UNDERLYING LAYER OF PROTECTION. OUR GOAL IS A FUNDAMENTAL TRANS-FORMATION IN THE DEGREE OF OPENNESS OF THE JAPANESE MARKET. WE ARE LOOKING FOR CONCRETE RESULTS, MEASURABLE BY INCREASED SALES OR MARKET SHARES FOR FOREIGN PRODUCTS.

EACH TEAM IS BEING LED BY AN UNDERSECRETARY TO ENSURE CONTINUAL HIGH-LEVEL INVOLVEMENT. THE PRESIDENT AND THE SECRETARY OF STATE, AS WELL AS AMBASSADOR BROCK, AND SECRETARIES BALDRIGE AND BLOCK WILL FOLLOW THE PROGRESS OF THESE NEGOTIATIONS AND

WILL REVIEW THEM WITH PRIME MINISTER NAKASONE AND APPROPRIATE MEMBERS OF HIS CABINET DURING THE COMING MONTHS. NO FINAL CUT-OFF DATE HAS BEEN SET FOR THESE DISCUSSIONS, BUT CERTAIN CHECKPOINTS SUGGEST THEMSELVES. IN THE TELECOMMUNICATIONS SECTOR, FOR EXAMPLE, SOME LIBERALIZATION IN MARKET ACCESS IS SCHEDULED TO OCCUR APRIL 1. BY THAT DATE WE WILL HAVE A REASONABLE FIX ON THE GROUND RULES UNDER WHICH U.S. SUPPLIERS OF TELECOMMUNICATIONS SERVICES AND EQUIPMENT WILL BE ABLE TO COMPETE IN JAPAN. THE BONN SUMMIT IN MAY OFFERS AN OPPORTUNITY FOR THE PRESIDENT AND THE PRIME MINISTER TO REVIEW THE PROGRESS MADE IN ALL THE SECTORAL DISCUSSIONS.

SECTORAL NEGOTIATIONS IN PROGRESS

TO DATE, MEETINGS HAVE BEEN HELD COVERING THREE OF THE FOUR SECTORS INITIALLY SELECTED FOR NEGOTIATIONS.

Telecommunications

WE HAVE MET TWICE TO DISCUSS TELECOMMUNICATIONS. UNDERSECRETARY OLMER WAS IN TOKYO THIS WEEK TO CONTINUE THOSE TALKS, WHICH WE WILL RESUME NEXT WEEK. IN ADDITION, TECHNICAL EXPERTS FROM USTR AND THE DEPARTMENT OF COMMERCE HAVE BEEN IN JAPAN FOR MORE THAN TWO WEEKS, KEEPING BEFORE THE JAPANESE OUR CONCERNS AND THOSE OF OUR COMPANIES AS ORDINANCES ARE DRAWN UP TO IMPLEMENT THE NEW TELECOMMUNICATIONS LAWS. IT'S TOO EARLY TO KNOW WHETHER THE "NEW" NTT WILL GIVE OUR EXPORTERS THE KIND OF ACCESS THEY OUGHT TO HAVE TO JAPAN'S TELECOMMUNICATIONS MARKET. WE'RE MAKING

SURE THAT JAPAN HAS OUR VIEWS, AND IT IS CLEAR THAT THE ORDINANCES WHICH EMERGE APRIL 1 WILL BE SEEN AS AN INITIAL TEST OF JAPANESE INTENTIONS. WHILE IN THE NEAR TERM OUR ATTENTION IN THIS SECTOR IS FOCUSED ON NTT AND VALUE-ADDED NETWORKS, WE ARE MEETING WITH U.S. INDUSTRY TO DEVELOP AN AGENDA FOR POST APRIL 1 NEGOTIATIONS, WHICH WILL ADDRESS THE OTHER OBSTACLES THAT CONFRONT OUR EXPORTERS IN THIS SECTOR.

Forest Products

AS YOU MAY KNOW, UNDERSECRETARY AMSTUTZ HELD A MEETING ON FOREST PRODUCTS IN JAPAN FEBRUARY 25. IN THAT SESSION HE EXPLAINED OUR VIEW AND THE VIEW OF OUR FOREST PRODUCTS INDUSTRY THAT TARIFFS ARE THE MOST IMPORTANT OBSTACLE WE NOW FACE IN THIS SECTOR. UNFORTUNATELY, THE JAPANESE SIDE REFUSED TO CONSIDER THE POSSIBILITY OF TARIFF CHANGES, A POSITION WE CONSIDER INCONSISTENT WITH THE MUTUAL UNDERSTANDING ON WHICH THESE NEGOTIATIONS ARE BASED. WE ARE NOW CONSIDERING STEPS TO MOVE THE WORK OF THIS TEAM AHEAD.

Electronics

WE HAVE HAD ONE MEETING WITH THE JAPANESE ON ELECTRONICS UNDER THIS NEW APPROACH. MANY OF THE PROBLEMS IN THIS SECTOR ARE FAMILIAR TO US FROM EARLIER DISCUSSIONS, FOR EXAMPLE IN THE U.S. - JAPAN HIGH TECHNOLOGY WORK GROUP. IN THE PAST WE HAVE HAD SOME SUCCESS IN THIS AREA, AS IN THE MUTUAL ELIMINATION OF SEMICONDUCTOR TARIFFS. WE EXPECT TO MEET AGAIN LATER IN MARCH. OUR AGENDA FOR THESE DISCUSSIONS IS BEING DEVELOPED IN CLOSE CONSULTATION WITH PRIVATE INDUSTRY.

Medical Equipment and Pharmaceuticals

NEXT WEEK WE WILL MEET IN JAPAN TO DISCUSS THE MEDICAL EQUIPMENT AND PHARMACEUTICALS SECTOR. A GOOD DEAL OF PRELIMINARY WORK HAS BEEN DONE IN THIS AREA OVER THE PAST FEW YEARS, PARTICULARLY ON PROBLEMS RELATED TO STANDARDS AND CERTIFICATION, ACCEPTANCE OF CLINICAL TEST DATA AND REGULATORY ISSUES. WE HAVE BEEN MEETING WITH PRIVATE INDUSTRY HERE, AS WELL AS TALKING WITH THE U.S. FIRMS THAT ARE REPRESENTED IN TOKYO, TO GET A CLEARER UNDERSTANDING OF HOW THIS SECTOR OPERATES IN JAPAN. WE NEED TO UNDERSTAND HOW THE PROBLEMS OUR COMPANIES FACE EACH STEP ALONG THE WAY, THAT IS, AT THE BORDER, IN PRODUCT APPROVAL, IN MANUFACTURING AND IN DISTRIBUTION, FIT INTO THE SECTOR AS A WHOLE. IN THIS WAY WE HOPE TO AVOID THE PITFALL OF GETTING MIRED DOWN IN A SPECIFIC PROBLEM AREA AND LOSING SIGHT OF THE BROADER GOAL OF OPENING UP THIS ENTIRE SECTOR.

ADDITIONAL NEGOTIATIONS IN PROGRESS

ALTHOUGH THE SECTORAL NEGOTIATIONS INITIATED BY PRESIDENT REAGAN AND PRIME MINISTER NAKASONE CAN BE, AND I EXPECT WILL BE, EXPANDED TO INCLUDE OTHER AREAS, IT IS NOT INTENDED TO SUBSTITUTE FOR ALL THE OTHER TRADE NEGOTIATIONS WE ARE CONDUCTING WITH JAPAN. NEXT WEEK I WILL CHAIR A MEETING OF THE U.S. - JAPAN TRADE COMMITTEE, IN WHICH WE WILL PURSUE A BROAD RANGE OF MARKET ACCESS ISSUES. THE AGENDA FOR THAT SESSION WILL INCLUDE TARIFFS, SERVICES, TOBACCO, GATT DISPUTES AND STANDARDS ISSUES, AMONG OTHER MATTERS.

WE WILL BE REPEATING OUR REQUESTS FOR TARIFF CUTS ON A WIDE RANGE OF ITEMS, INCLUDING ALUMINUM, CHOCOLATE CONFECTIONERY, FRESH GRAPEFRUIT AND WALNUTS, PHOTOGRAPHIC FILM, ARAMID FIBER AND WINE.

OUR SERVICES DISCUSSIONS WILL COVER, AMONG OTHER TOPICS, THE CONDITIONS UNDER WHICH U.S. LAWYERS CAN PRACTICE IN JAPAN.

JAPAN'S TOBACCO AND SALT MONOPOLY IS BEING PRIVATIZED. WE HAVE BEEN WORKING CLOSELY WITH OUR TOBACCO PRODUCT EXPORTERS AND WITH THE JAPANESE GOVERNMENT TO TRY TO ASSURE THAT OUR COMPANIES WILL HAVE A FAIR CHANCE TO COMPETE UNDER THE NEW ARRANGEMENT.

AMONG THE GATT ISSUES WE'LL DISCUSS WILL BE JAPAN'S COMPLIANCE WITH A PANEL DECISION WHICH FOUND JAPANESE IMPORT QUOTAS IN THE LEATHER SECTOR TO BE IN VIOLATION OF THE GATT.

AS YOU SEE, MR. CHAIRMAN, OUR PRESENT TRADE DIALOGUE WITH JAPAN SPANS NEARLY THE WHOLE RANGE OF OUR TRADE RELATIONSHIP. THE FOCUS OF THAT DIALOGUE, INCLUDING THE HIGH-LEVEL SECTORAL DISCUSSIONS SET IN MOTION BY THE PRESIDENT AND THE PRIME MINISTER, AS WELL AS OUR TALKS IN THE TRADE COMMITTEE AND OTHER TRADE FORA, IS MARKET ACCESS. OUR GOAL REMAINS AN ACROSS-THE-BOARD REDUCTION IN THE BARRIERS OUR EXPORTERS FACE IN JAPAN, SO THAT THE OPPORTUNITIES U.S. COMPANIES HAVE TO SELL IN JAPAN ARE COMPARABLE TO

THOSE THAT JAPANESE COMPANIES HAVE IN THE UNITED STATES. THIS KIND OF OPENLY COMPETITIVE ENVIRONMENT WOULD BENEFIT CONSUMERS IN BOTH COUNTRIES AND PROVIDE THE STIMULUS NEEDED BY INDUSTRIES IN BOTH COUNTRIES. IN FACT, ONLY THIS KIND OF ENVIRONMENT CAN BE A BASIS FOR THE STABLE, TRANQUIL AND MUTUALLY PRODUCTIVE TRADE RELATIONSHIP WE SEEK WITH JAPAN.

Senator DANFORTH. Thank you, Ambassador Smith.
Secretary Olmer.

STATEMENT OF HON. LIONEL OLMER, UNDER SECRETARY FOR INTERNATIONAL TRADE, DEPARTMENT OF COMMERCE

Secretary OLMER. Thank you, Mr. Chairman, members of the committee. I would like to say, by way of preface, that the sustained intense interest of and pressure from this committee and the insights which each of you expressed I greatly admire and value and believe are essential to the process we have undertaken. As you know, I just returned from Tokyo the day before yesterday, after 2 days of intense discussions on the subject of telecommunications.

I have come to the conclusion—the unhappy conclusion—that absent significant changes in the next 23 days, a system will be put in place beginning on April 1, 1985, which seriously disadvantages all foreign suppliers, especially U.S. suppliers—because I believe we are far and away the most competitive potential suppliers of telecommunications and related products in the world—a system which furthermore does an injustice to Japanese consumers by denying them the freedom of choice and the freedom of a product at a low price, and which, finally, lends fuel to a growing, if not already hardened, international perception that despite political statements to the contrary Japan remains committed to keeping its market protected from foreign competition.

Now, on the 1st of April, we and others who desire to provide telecommunications services and products in Japan are going to confront a system with essentially the following characteristics: A system which is both cumbersome and inherently discriminatory for the purpose of registering something known as enhanced telecommunications services—and I am prepared to explain what that is in a few moments—a maze of various approving authorities in a variety of government ministries and then, depending on the specific piece of equipment and the type of approval, NTT itself—NTT, which is supposed to become privatized, will remain in control of something in the neighborhood of fifteen-sixteenths of the entire range of prospective equipment and services to be offered—a system of standard setting which is not transparent, and standards that go well beyond those which are required for the protection of the network, which are our standards. No adequate safeguards to prevent cross-subsidization by the once-powerful—and in my view, an institution that will remain very powerful in the Japanese system—Nippon Telegraph & Telephone Corp. The absence of standards to prevent its cross-subsidization, using its revenues to promote and encourage and nourish infant industries, and to prejudice those that seek to compete with those infant industries in Japan. In fact, NTT will begin this new process on the 1st of April, remaining in control of its own approvals. It will not have to submit its applications to an independent agency. Foreign suppliers, on the other hand, are going to have to begin at square one and submit information which may well indeed be of a proprietary nature before they get initial approval. At one point—and still on the written record—it was required that on the board of directors

of the approval agency there will be representatives of competing telecommunications companies.

Our suppliers will also have to go back to the Ministry of Post and Telecommunications if they desire to change any of the services for which they were given approval or to receive from that ministry additional import authority. That is to say, if they estimate they are going to sell 500 a month and suddenly the market expands beyond their expectations to 600 a month, they will be required to go back and through the reregistration process for the additional approvals for the additional 100 pieces of equipment. Finally, a telecommunications advisory council that will make, over time, key decisions of a policy nature on the entirety of the telecommunications industry, and that will not have not only any foreign representation but any representation from an American company which happens to have a Japanese national working for it in Japan. Now, in contrast, and I think it is always important to keep in mind that we are after reciprocity or relative equivalence, so we need to look at what we offer to foreigners who seek access to our market. In contrast, Japanese suppliers face a system in the United States which allows each and every Japanese supplier to self-certify its equipment according to published Federal Communications Commission requirements, which requirements are limited only by the criteria to prevent "harm to the network." A system that seeks to obtain in advance foreign input to the setting of standards, that is to say, a public comment period before new regulations and procedures take effect. And furthermore, and perhaps the most fundamentally important in the context of April 1, a system which leaves this new market for enhanced telecommunications services in our country totally unregulated. Attached to my testimony are graphs that explain this in some detail, and I have larger charts which perhaps are easier to see here. Now, before I invite your attention to these charts, Mr. Chairman, I would like to say just a few other words, and I think this perhaps picks up on what Senator Heinz referred to as some of the fundamentals. The contrasts reflect deep philosophic differences between our two countries. When we opened our telecommunications system to competition, we not only opened it to foreigners, we invited them in and the taxpayer of the United States pays to facilitate foreign-producer entry to our market. And we relied on market forces. Our regulations in fact are written to limit to the maximum extent possible the discretionary authority of bureaucrats. Now, we took these actions, in my judgment, based on a commitment to the principles of the free market, as an engine of technological change and to the private sector as the source of wisdom on the development of the marketplace.

The Japanese system does not do that. It makes little provision for foreigners to play a role. It does not sufficiently limit the power, the discretionary authority of its bureaucrats, and it allows little scope for the market. It thus, in effect, restricts the creativity not only of foreigners but of Japanese businessmen alike.

One of our first examples of the new approval system makes the point that protection against foreign competition and limits on technological change go hand in hand. An American company had applied to the Japanese Approval Institute to get a certification of

a modem, a device that fits between the incoming signal and a printer keyboard. Now, this modem had an automatic dialing function to remove the necessity of the operator from dialing up on the modem before it was connected. It saves a matter of seconds—no more than that. In mid-January, the Approval Institute informed the company's Japanese distributor that the modem could not be approved because the automatic dialing feature did not meet NTT's technical standards. That is because they have not yet developed any technical standards, and that is because there are no such modems sold in Japan.

Now, the American found out——

Senator CHAFEE. What are you suggesting there—that if the Japanese company had one, then it would meet the Japanese—the NTT's—technical standards?

Secretary OLMER. Senator Chafee, there could not be Japanese products sold unless there was a standard for it to meet. What would first be required is for the Japanese company to develop its product and to submit it to the approval agency and say: Here is a new device I want to sell. Will you write a technical standard for its approval for sale in the marketplace? And over a period of time, presumably, it could get that approval. At that point, there would be standards against which it could be measured. In our system, the absence of a technical standard would not be a bar to its entry, and I will make a further point that I think will go to your question, perhaps more directly. The American company then agreed to modify its product to remove this technological advantage, and has been given an indication by removing this technological advantage, it might receive approval. I received a phone call this morning expressing the great embarrassment of the approval agency, telling me that as of April 1 it would be approved in Japan, and it was a mistake to begin with. It shouldn't have been rejected.

The point I am trying to make by that one example—and we don't believe in totality the market for that device will exceed $1 million—is that we can't afford to go through each and every one of these things every time they arise. We don't have the resources for it, and American companies don't have the patience or the capital reserve to sit by and wait while the Government tries—sometimes succeeds, often times fails—to fix it for them.

Now, we have asked the Japanese Government—and I did so in the 2 days I spent in Tokyo, and I will be joining Mike next week again in Tokyo—we asked the Japanese Government to make certain necessary changes between now and the 1st of April—to in effect provide in Japan that which they have in the United States, and we haven't even gone to the degree of saying you must mirror-image it. We are willing to make some recognized exceptions for differences in the nature of the telecommunications system. We want them to eliminate the preregistration system for the kind of telecommunications service we think most American companies would like to offer. We want participation by foreign experts in their telecommunications advisory council, and we want a single, independent—truly independent—approval agency for all equipment which will attach to the telecommunications network. We want an opportunity for foreign comment on proposed standards, and we want to limit standards requirements to those applicable to

the integration and to the question of harm to the network. We furthermore have said that it is essential that we receive self-certification authority by our suppliers to tell us the standards which must be met and allow them to certify they will meet those standards. In some 9 years of FCC practice in this regard, there have been only seven cases, I am told, where the FCC has asked to receive a particular product in challenging an applicant's submission—its own certification. And harm to the network in those 9 years has not resulted, and that entire system is run by three people in Washington. As of this morning, the recommendations that I have just referred to have not been incorporated in the ordinances that are being issued by the Ministry of Post and Telecommunications. We have technical negotiators who remain in Japan, trying to work this out. And as I have indicated, Mike and I will be back there next week. We remain hopeful that, given the seriousness of the situation, we will reach our objectives.

Now, what I have tried to do in this chart, Mr. Chairman, in two separate charts, is to provide you with an idea of the variety—and this is an attachment to the testimony—of telecommunications services which are going to be offered and to contrast the regulatory system being put in place as of April 1 with what is available to all foreign suppliers in the American system. And much like the charts you displayed of the trade imbalance, you will note the paucity of registration requirements on the far right in contrast to the requirements of the Japanese on the left.

One final comment, Mr. Chairman, before I try to answer any questions you and the members might have. I left with the Vice Minister of Post and Telecommunications a letter. I happen to believe it is a thoughtful letter, not a provocative letter, but a letter which, in keeping with the spirit that you announced at the beginning, doesn't express anger, it just expresses the seriousness of our purpose and what it is we are seeking to achieve. I would like to introduce that letter to the record as an attachment to my testimony.

Senator DANFORTH. Fine. It will be included in the record.

[Under Secretary Olmer's prepared statement and letter follows:]

PREPARED STATEMENT OF UNDER SECRETARY OF COMMERCE LIONEL H. OLMER

I welcome this opportunity to testify on the current state of U.S.-Japan trade relations. I have just returned from Tokyo where I chaired a two day meeting of the sectoral group discussing access to the Japanese telecommunications market. These discussions are based on the commitment to maintain an open market in telecommunications equipment given by Prime Minister Nakasone to President Reagan at the January 2 summit. Although telecommunications represents a fraction of our total trade, the issue is a watershed in our relationship.

After well over a year of discussion, I have come to the conclusion that, absent significant changes in the next twenty three days, a system will be put in place beginning on April 1, 1985:

-which seriously disadvantages foreign suppliers,
-which does an injustice to Japanese consumers, and
-which lends fuel to a growing international perception that, despite political statements to the contrary, Japan remains committed to keeping its market protected from foreign competition.

Specifically, on April 1, U.S. and other foreign suppliers will face a system with the following characteristics:

-A cumbersome and inherently discriminatory system for registering enhanced communications services;

-A potential maze of approving authorities--JATE, MITI and NTT itself--to approve equipment for attachment to the network. Depending on the specific piece of equipment, the array of required approvals would differ. NTT would control approval of digital equipment.

-Non-transparent standards setting, and standards which go beyond those required for integration and protection of the network.

-No adequate safeguards to prevent the only current Class I carrier, NTT, from using its revenues to cross-subsidize services in which it faces competition. Indeed, NTT will start out with automatic approval for its services. Potential foreign competitors will have to begin at square one, and submit information which may be confidential, before they get initial approval. They would also have to go back to MPT for any change in service.

-A Telecommunications Advisory Council, which will make key policy decisions on the telecommunications industry, which will not have any foreign representatives and which may well have vested interests of one sort or another to Japanese telecommunications manufacturers.

In contrast, Japanese suppliers face a system here in the United States which:

-Allows Japanese suppliers to self-certify their equipment to FCC requirements, which are limited to those needed to prevent harm to the network;

-Seeks foreign input on standards decisions through a well-established system of prior notification and public hearings;

-Leaves enhanced telecommunications services totally unregulated.

This contrast is graphically illustrated in the attachments to this statement.

These contrasts reflect deep philosophical differences between the United States and Japan. When we opened our telecommunications system to competition, we included foreign competitors. We relied on market forces. We wrote our regulations to limit to the maximum extent possible the discretionary authority of personnel in the agencies charged with their administration.

We took these actions based on our commitment to the market as an engine of technological change, and to the private sector as the proven source of business wisdom.

The Japanese system will not do that. It makes little provision for foreign competitors to play a role. It does not sufficiently limit the discretion of its bureaucrats. It allows little scope for the market. It restricts the creativity of foreign and Japanese businessmen alike.

One of our first examples with the new approval system makes the point that protection against foreign competition and limits on technological change go hand in hand. An America company has applied to JATE for approval of its modem, which has an automatic dialing function. In mid-January, JATE informed the company's Japanese distributor that the modem could not be approved because its automatic dialing feature did not meet NTT's technical standards. The key point here is that no Japanese company now offers a modem with this feature. The American company has agreed to modify its product, and thus to sacrifice a feature which was a substantial competitive advantage.

I submit that we are not off to a good start.

We are still actively negotiating with the Government of Japan to make the necessary changes in this system between now and April 1 which will:

-Eliminate the notification/registation system for Special Type II Value Added Networks, and ultimately eliminate the arbitrary distinction between VAN services above 500 lines/1200 BPS;

-Allow participation by foreign experts on the Telecommunications Advisory Council;

-Establish a single independent approval agency for all customer premise equipment, for attachment to all telecommunications networks;

-Provide an opportunity for foreign comment on proposed standards, and limit standards requirements to those applicable to integration and harm to the network;

-Allow self-certification by foreign equipment suppliers.

-Establish accounting procedures which guard against cross-subsidization by NTT.

As of this morning, these recommendations have not been incorporated in the ordinances of the Ministry of Posts and Telecommunications. Our negotiators remain in Tokyo still trying to achieve these results. I will return to Japan next week and remain hopeful that, given the seriousness of this situation, we will reach our objectives.

45-934 O—85——4

[illegible]
(Effective April 1, 1985

JAPAN			UNITED STATES
REGULATED		LESS REGULATED	
TYPE I (Owns Facilities)	SPECIAL TYPE II (Leases Lines From Type I Carrier)	GENERAL TYPE II (Leases Lines From (Type I Carrier)	LEASED LINE ENHANCED SERVICE PROVIDERS
Classification Criteria: - owns facilities	Classification Criteria: - open network ("many and unspecified") - above 500 lines/ 1200 bps - international communication links	Classification Criteria: - closed network ("specified customers")	Classification Criteria: - provides enhanced services across leased lines
Regulatory Constraints: (Major Items) - prior permission from MPT* based on: -- business plan -- financial projections -- proven technical ability -- detailed network information -- detailed information on services provided - tariff authorized by MPT* - facilities must conform to broad technical standards set by MPT* - administrative rules of business approved by MPT* - required to have a licensed Chief Engineer - must apply for permission for service and network changes	Regulatory Constraints: (Major Items) - prior registration based on: -- business plan -- financial projections -- proven technical ability -- detailed network information -- detailed information on services provided - tariffs notified to MPT - facilities must conform to broad technical standards set by MPT* - administrative rules of business approved by MPT* - required to have a licensed Chief Engineer - must apply for registration of service and network changes --- below 500 lines/1200 bps same as General Type II	Regulatory Constraints: (Major Items) - prior notification - submit notification of change on: -- name and address -- services offered	Regulatory Constraints: (Major Items) - no prior approval - no notification of information - applies to foreign & domestic suppliers

*MPT: Ministry of Post and Telecommunications

JAPAN

TYPE I

Services Offered:
(Examples)

- basic switching and and transmission
- voice transmission:
  -- telephone
- image transmission:
  -- facsimile
  -- videotex
- data transmission:
  -- packet switching
- other VAN** application:
  -- timesharing
  -- remote database
  -- "mailbox"
  -- distributed data processing

Special Type II

Services Offered:
(Examples)

- basic switching and and transmission
- voice transmission:
  -- telephone
- image transmission:
  -- facsimile
  -- videotex
- data transmission:
  -- packet switching
- other VAN** applications:
  -- time sharing
  -- remote database
  -- "mailbox"
  -- distributed data processing

General Type II

Services Offered:
(Examples)

- basic switching and and transmission
- voice transmission:
  -- telephone
- image transmission:
  -- facsimile
  -- videotex
- data transmission:
  -- packet switching
- other VAN** applications:
  -- timesharing
  -- remote database
  -- "mailbox"
  -- distributed data processing

United States
Enhanced Service provider

Services Offered:
(Examples)

- full-range of value added network and enhanced service applications

** VAN: Valued-Added Network

Tokyo, Japan

March 5, 1985

The Honorable Moriya Koyama
Vice Minister
Ministry of Posts and
Telecommunications
1-2, Kasumigaseki 2-chome
Chiyoda-ku, Tokyo 100

Dear Vice Minister Koyama:

I want to thank you for the time and the great effort that you and your staff have given to our mutual efforts to discuss the application of Japan's new telecommunications law which becomes effective on April 1, 1985.

I believe that our efforts have resulted in some progress, although I am sure that you agree we have much further to go to resolve all problems.

I am sure that you share my desire that Japan create a telecommunications environment as free of unnecessary barriers as is possible. It is in the interest of achieving this objective that I make these comments, for my own careful review of our mutual efforts to date reveal that, if left untouched by your personal intervention, a system will be put in place beginning on April 1, 1985, which seriously disadvantages foreign suppliers, does an injustice to Japanese consumers and lends fuel to an international perception that, despite political statements to the contrary, Japan remains committed to keeping its market essentially protected from foreign competition.

Our two governments have been discussing some of the outstanding issues in the telecommunications sector for more than a year. This is particularly true of the issues concerning the notification and registration of Type II telecommunications enterprises. A year ago, the U.S. Government pointed out, in the strongest possible terms, that registration and notification procedures could become barriers if they were to include a prior approval process.

At that time, your Government provided assurances that such procedures would be simple and automatic and that applications would be rejected only in very unusual circumstances to be established by law.

However, after examination of the actual law and discussions with your Government concerning the pertinent Cabinet and Ministerial ordinances, our original concerns have become amplified. The proposed procedures require a great deal of seemingly unnecessary information and, in instances, business-confidential data; they also appear to contain an obligation to obtain prior approval at various levels of the Japanese Government.

Accordingly, I hope that, as a result of our discussions, you will be able to simplify the procedures and to make them automatic and, thus, eliminate the need for prior approval. Also, to ensure transparency, I propose that you create an appeal channel and periodically review established procedures.

I believe that you also are aware that we have been concerned for some time with the distinction between "general" and "special" Type II telecommunications enterprises -- specifically, the use of 500 lines and 1200 bits per second (BPS) as one of the criteria to distinguish between the two categories. We believe that the use of this criterion may impede technological development within Japan's telecommunications sector. For example, how will your Government handle the classification issue when, in the very near term, the use of fiber optic systems increases dramatically in Japan?

Similarly, we are concerned with the definition of an "unspecified" number of customers which also will serve as a criterion to distinguish "general" from "special" Type II enterprises. I hope that you will be able to define "unspecified" more clearly and to confine such a criterion predominantly to voice transmission. As with the 500 lines/1200 BPS criterion, it would be preferable not to use an arbitrary, numerical calculation to determine the meaning of "unspecified."

In the area of standards and certification, you know that we are concerned with the potential for trade barriers to arise in the future. To avoid potential problems, I believe it is

essential that only one independent approval agency be responsible for certifying all "customer premise equipment" for attachment to all telecommunications networks. This means that NTT would not have the authority to certify equipment for itself or for any other company.

I also believe that, in accord with the GATT Standards Code and the Gotoda Commission Report of 1983, MPT should provide ample opportunity for comment on the draft standards and rules for approving equipment, which were made available only last week.

Regarding the standards, they should be established solely to prevent harm to the network.

Another issue of longstanding concern is the potential for cross subsidization between communications services that will be offered by NTT after April 1, 1985. I know that you also are concerned about this problem. I trust that you will do your best to prevent any such possibility through the establishment of strict accounting and other procedures within NTT. Safeguards against cross subsidization within NTT should be guaranteed in order to ensure full competition in the new telecommunications environment which you are creating. We have provided your staff with a listing of specific measures to guard against cross subsidization, based on our experience with telecommunications development in America.

Finally, there remains the question of representation on advisory councils. This difficult issue has been addressed in other bilateral discussions. I understand that the members of a council are chosen for their experience in and knowledge of a particular sector. Accordingly, Japanese nationals working for foreign-affiliated telecommunications companies in Japan should have an opportunity to bring their special knowledge to advisory councils which consider telecommunications issues. Therefore, I urge you to provide for membership for such persons on all relevant advisory councils.

I would also like to point out that under the U.S.-Japan High Technology Agreement of 1983, Japan agreed to make efforts to ensure that the representatives of such foreign-affiliated companies serve on all committees which develop policy or draft standards in the high-technology field. I trust that you will ensure that this commitment is met in the telecommunications sector.

An objective within my government has been to write laws, and the regulations for their implementation, which limit to the maximum extent possible the discretionary authority of personnel in the agencies charged with their administration. One reason for this objective is to provide the private citizen falling under these laws with the maximum degree of certainty and predictability and to reduce his dependency on the whims of bureaucrats who can often interpret laws to suit transient interests. My feeling on the development of your implementing directives is that they do not yet go far enough in the direction of limiting discretionary authority. I believe firmly that they must, if we are to achieve our objective of an open telecommunications market.

I am looking forward to our working together to promote competition and innovation in this most vital sector which links our two countries. However, time is growing short and it is obvious that the pressure on both of us to succeed is intensifying.

Sincerely yours,

Lionel Olmer
Under Secretary of Commerce
for International Trade

Senator DANFORTH. Gentlemen, thank you very much. Let me tell you what I think the position of the administration with respect to the voluntary restraint agreement nonextension says. I think that the message has to do with the general trade policy of the administration. This will sound like a caricature of a position, but I really think it is a fair characterization. And I want you to respond to it.

I believe that the administration's position is this: Regardless of the bilateral trade deficit with Japan and regardless of any unfair trade practices by the Japanese, the administration will work to expand Japanese access to United States markets and will not retaliate against Japanese unfair trade practices. Now, would that be an accurate description of the administration's policy?

Secretary OLMER. I would like to defer to our Deputy Chief Trade Policy negotiator, and all-around factotem. [Laughter.]

Ambassador SMITH. Mr. Chairman, as you know, I have some sort of kinship to sailboats, and quite frankly, rather than answering that question, I would rather be sailing. [Laughter.]

I don't think that is a fair characterization, sir. We are not trying to increase or working toward the increase of Japanese access into the United States market. Certainly that hasn't been my marching orders for some 3 or 4 years. To the contrary, I think for the whole panoply of Government officials who have, as you pointed out, made so many trips back and forth to Tokyo, our overriding objective has been to increase United States access into the Japanese market. By this current sectorial approach that we have been working on for the past 6 weeks, we have made clear to the Japanese—the President made clear to Prime Minister Nakasone, and Secretary Wallace made clear at the opening session to his counterpart—that this is not the normal sort of negotiation. We are not trading off access here for access there. We are, if you will, enlisting their help, if we can get it, in helping us to identify the barriers——

Senator DANFORTH. Let me put the question this way: Is it not the policy of the administration that, regardless of what the Japanese do to us, we will never retaliate?

Secretary OLMER. No, I don't believe that's so.

Senator DANFORTH. Would you please tell the committee—the subcommittee—any examples you can think of when the United States has retaliated against Japan?

[Long silence.]

Ambassador SMITH. We have in cases where there is a dispute which has not been able to be resolved, in one form or another, taken them to the GATT, and we have a case outstanding with them in which they have accepted the verdict. that they are acting inconsistent with the GATT. On March 12, this issue will be raised again in the GATT, asking for their report, which they must make to the contracting parties as to what they have done. I cannot, however, in the time that I have been in Washington, sir, give you an example of where we have "retaliated." But we have been involved in intensive negotiations on a wide variety of issues——

Senator DANFORTH. I know we have negotiated. The problem is that is all we do—we talk. Now, let me ask you this. How many

times have each of you in the last 4 years been to Tokyo for trade talks? Approximately?

Ambassador SMITH. Since I started in the trade business, Senator, in 1973, I have made 51 trips to Tokyo.

Senator DANFORTH. Whew! Secretary Olmer?

Secretary OLMER. I guess that in the last 4 years I have made 15 trips. Could I comment on your first question?

Senator DANFORTH. Surely.

Secretary OLMER. I think that, rather than use the term "retaliation," it is a fact that the Japanese have cooperated with us in a number of areas in the trade field that we have asked for their cooperation, such as automobiles. And such as steel. And such as beef and citrus. I believe that to be a marginal concession on their part, but there have been a number of areas in which they have supported us in international fora on trade policy issues, support for a new round of the GATT, and so on. So, I think if you use the word "retaliation," you are probably right—we haven't retaliated.

Senator DANFORTH. Right. I mean, obviously, I suppose there are examples when they could do even worse to us than they have done, and when they could do even worse to the world than they have done, but the fact of the matter is that they do use unfair trade practices, and we don't retaliate, and that is our policy. I take it that while you two have made many trips to Tokyo, it would also be true that there have been as many occasions when Japanese officials have come to Washington to negotiate with you. Is that right?

Ambassador SMITH. Yes, sir.

Senator DANFORTH. A long history of discussions. The President—or the administration, I guess it was Mr. Speakes—stated at the time of the announcement of the administration's position on VRA with respect to cars that the hope was that the Japanese would be encouraged to open their markets. In other words, our position with respect to increased access to the U.S. market for Japanese automobiles would result in greater access to the Japanese market of what we produce. If that is the administration's policy, would the administration be willing to give us a written report every 3 months as to how that policy is working out?

Ambassador SMITH. Mr. Chairman, the President decided not to ask Japan to continue its restraints. I would not say, sir, that the request or the statement of the President that we would not ask the Japanese for a fifth year was a direct quid pro quo.

What we have said was that we have set an example for a variety of reasons which were explained by the President and Mr. Speakes—by deciding not to seek a fifth year. There remains the fundamental problem, however, which has been plaguing us both before, during, and now since the automobile restraints regarding access to the Japanese market. That is the fundamental problem that we must address.

Senator DANFORTH. Would you be good enough to give us a report from the administration as to whether the position of the administration with respect to VRA's is yielding some reciprocal fruit? I mean, I want to see what happens on the other side.

Ambassador SMITH. Mike may want to respond, Mr. Chairman in general to that question, but I could give you a specific.

Senator DANFORTH. All I want is a letter every 3 months that tells us how we are doing and whether or not the Japanese are opening their markets in response to our, I think very generous act. I mean, when you consider a $37 billion trade deficit, for us to say all right and here is another $4, $5, $6 billion or whatever it is of additional sales that you are going to have a year to the United States, and our hope is that you will open our market—I think that we should at least be keeping tabs on whether that hope has any substance.

Ambassador SMITH. Senator, I am sure that we would be pleased not only to send you a letter every 3 months but if you would like one every month, we would be glad to do that too.

Senator DANFORTH. Whatever we can work out, but I want to know. Obviously, I don't mean to badger the two of you. I would never badger anybody as slim and trim as you are. [Laughter.]

And I don't, as you know, mean it that way. I have the greatest respect for both of you. I think you are outstanding. The problem is not with you. The problem is with Japan, and I just think what we are doing is complaining and that is about it and that the negotiations really aren't hitting anywhere. The time has come to do something.

Secretary OLMER. Could I just say something about your desire for a standard against which to measure performance? The first of April is going to provide you with exactly that opportunity. This is very different from things which we have undertaken before, not necessarily with respect to the manner in which we are approaching it but in the fact that the Japanese system is changing, without a shadow of a doubt. And if things don't change in the next 23 days in ways which we have already described to them in exhausting detail, you will have a standard against which to measure a response required by us to that.

Senator BRADLEY. Mr. Chairman, could he expand on that just a little bit? What happens April 1?

Secretary OLMER. On April 1, Senator Bradley, the Japanese will implement a new law which has as its purpose the creation of a private telecommunications system. They have a law, and then they have implementing regulations which they call ordinances, and then they have ministerial guidelines which are also written instructions to the bureaucrats to implement the ordinances which implement the regulations. We have asked for a year for access to those written ordinances, and we just received almost all of them—not quite all of them—this past week. Our analysis of them remains incomplete, but to the extent we are able to piece together what they are intending to do, I have demonstrated on these charts and in the attachment to the testimony it will have the effect of severely prejudicing any foreigner's access into the Japanese market. It is going to be the world's second largest market for telecommunications products, and it represents something different in this respect. We have always tried to play catchup. We have always gone to them and said: Would you please undo what you have done? Would you please fix this trade problem that an American supplier has brought to our attention? Here is the first instance that I can recall in which we are there at the beginning

before they get started, and if we fail to do what is right by the American supplier, I think we deserve what we get.

Senator DANFORTH. Senator Bentsen?

Senator BENTSEN. Thank you very much, Mr. Chairman. Let me say, Mr. Olmer, when you said it was just a marginal gain insofar as beef and citrus, that was certainly true. When it comes to beef, all we gained was a "quarter pounder" there. [Laughter.]

When it comes to citrus, the Japanese went to domestic content. They said that you had to blend Japanese juice with the import. Now, there is no question in my mind but what these two great nations—the two most advanced technologically in the world with so much to learn from each other—are tragically on a collision course. And I know of no nation that is more vulnerable to a binge of protectionism in this world than is Japan, a country that thinks it is strong because it has that kind of a trade surplus. It has fueled over 40 percent of its growth since 1979 from exports. That nation is really not interested in free trade if the way they have been pursuing it is any guide. What they are interested in is a free hand, and that is the way they have dealt with us. Now, I don't think we are going anywhere with these negotiations that seriously counts. And my friend over here, the chairman, is from Missouri, and I am from Texas and I am proud to be a Texan, but at the moment I very much envy the slogan of Missouri—show me—and I think that is what we should do. Let them show us they are opening their market, because I don't think the negotiations are really gaining anything. Any time we have a situation where we have the most advanced communications system in the world and we have a $900 million trade deficiency with the Japanese on communications equipment, that tells me something.

When I hear what you have just said about now that the communications system is going into the private sector, and yet they are writing the regulations that will probably be even tougher than what we face now, the Japanese are asking for real trouble, not just from us, but from around this world. And it is not in their best interest. Do you know any nation in the world that is more vulnerable to protectionism than the Japanese?

Secretary OLMER. No, sir.

Senator BENTSEN. Thank you very much, Mr. Chairman.

Senator DANFORTH. Senator Bradley?

Senator BRADLEY. I would like to get some sense of how the decision was made on the VRA's on autos. What was the State Department contribution to this decision?

Ambassador Smith. Senator, neither Mr. Olmer nor I were at all the meetings at cabinet level in which the automobile issue was discussed. I can't tell you 100 percent what the State Department position was, not working for them, but I believe that their view had been rather consistently that they thought the time had come when the President should not seek a fifth year. I believe that was the State Department's position, sir.

Senator BRADLEY. So, the USTR and the State Department agreed with the decision not to seek a fifth year and Commerce did not agree.

Secretary OLMER. No, sir. To the best of my knowledge and belief, as we lawyers say, Senator Bradley, I would submit that not

a single agency dissented from the recommendations that went forward and that the recommendations in sum reflected an economic judgment—that it was simply in the interest of a larger number of American citizens that the restraint be removed, No. 1. That was of overriding significance—that the economics simply didn't warrant the continuation of the restraint.

And No. 2, that it certainly was in keeping with the administration's desire to maintain a nonprotectionist trade policy.

Senator BRADLEY. So, it was the unanimous administration position?

Secretary OLMER. To the best of my belief. Yes, sir.

Senator BRADLEY. Today in response to the committee's questioning, Mr. Olmer, I heard in your responses that you felt that the April 1 deadline—how the Japanese treated the access to their telecommunications market of different U.S. products—was a very important issue. I might have read a little bit too much into what you said, but might the administration reconsider their position on automobiles if indeed the Japanese do not open up much more on telecommunications?

Secretary OLMER. I do not believe so, and if I were asked for a recommendation, I would argue that there should be no change in the VRA judgment, that the VRA issue stands on its own and that we would be more harmed than helped by linking the two. What the Japanese need to do in telecommunications, they need to do in telecommunications period.

Senator BRADLEY. And it is your judgment that they are likely to open up more. Is that correct?

Secretary OLMER. In telecommunications? We have characterized the issue to them in such a serious way, I find it difficult to believe that we are not going to succeed. We have made some progress, and I haven't had time to go into some of the things where they have been responsive to us, but you always run a risk. I announced in Japan at a press conference the day before yesterday that I was encouraged, but believed that we still had a long way to go. When I got back to Washington, I was telephoned and told "You have given away the store. The Japanese have taken your word that progress has been made to be consonant with the view that they don't have to do any more." Which is one reason why I have tried to sound a little tough here today, to reverse that perception. [Laughter.]

Senator BRADLEY. I think the committee succeeded. One last question. Do you anticipate seeking a reduction in the Japanese tariff on chocolate imports? It is the highest in the world.

Ambassador SMITH. Senator Bradley, we have had that on our normal trade committee work now ever since I have been involved, which is 2 years. The current duty is 20 percent. We have made a request to the Japanese that the duty be reduced to our level of 7 percent in a 2-year period—to go from 20 to 10 and then 10 to 7. The Japanese in their last deliberative council on December 18, or something like that, did not accept that request. I have therefore told the Japanese that on Monday morning Tokyo time, chocolate is back on the list, and we reiterate our request that the duty for chocolate be reduced. I have been in consultation with the confectionery industry on this.

Senator DANFORTH. Senator Chafee.

Senator CHAFEE. Thank you, Mr. Chairman. Gentlemen, I want to say that I think the administration did exactly the right thing in lifting the voluntary restraints on Japanese automobiles, those that cost U.S. consumers, as you note in your statement, Mr. Ambassador, $16 billion over the last 4 years. The American industry last year made a $10 billion profit, and what you did is strike a great big blow for the American automobile consumer, and I think that was right. As I mentioned earlier, I don't think there is any questioning of restriction of the automobile market in Japan to U.S. automobiles. I am not sure we could sell many there anyway. I don't know exactly what the market is, but I have never heard complaints from automobile manufacturers on that score. Now let's look at this April 1 deadline.

First, you mentioned the elimination of the semiconductor tariffs. Now, how does that work out?

Ambassador SMITH. The two sides, Senator, have agreed to and have exchanged letters to eliminate the duty on semiconductors pursuant to the 1984 Trade Act.

Senator CHAFEE. But we don't know whether we have been able to sell our semiconductors there, do we?

Ambassador SMITH. Yes. We sell semiconductors there, and obviously, the Japanese sell semiconductors here. Right now, I believe the balance of trade is in the Japanese favor on this issue.

Secretary OLMER. Could I make a comment on that?

Senator CHAFEE. Yes.

Secretary OLMER. The major reason U.S. semiconductor manufacturers advanced this proposition, which the Government endorsed, was so that they would save tariffs on the reimportation of partially assembled semiconductors from their plants in Southeast Asia. Very few U.S. semiconductor manufacturers believed that this would vastly increase their market access in Japan, and some of them recently have said that as soon as the shortage of semiconductors in Japan went away—that is, Japanese manufacturers were able to supply the quantities required by the manufacturers of electronic equipment and computers—that those manufacturers resorted to their old-time Japanese suppliers. The U.S. semiconductor industry has had roughly 10 percent of the Japanese market for many, many years, and it hasn't altered despite the change in the dollar-yen ratio, and in my view, it is not going to change dramatically, maybe not even marginally, by the elimination of the tariff—that is between the two of us—but it is going to save——

Senator CHAFEE. Will it result in a deluge in the U.S. market?

Secretary OLMER. It could very well increase the Japanese access in the American market. They have never had any problem, however, dropping their price to suit the conditions in the market at the time, but in any event, we will give them a windfall opportunity, I think.

Senator CHAFEE. Now, Senator Bentsen in his remarks said that the amount of the Japanese share of our telecommunications market—he said that there was a $900 million differential between what we sell there and what they sell here. About $1 billion—does that sound right?

Secretary OLMER. I think it might be a little more than Senator Bentsen said.

Senator CHAFEE. The differential?

Secretary OLMER. Yes, the differential.

Senator CHAFEE. I am not going to quibble, but roughly it is in that area. Now, what I am concerned about is that they will nickle and dime us as we move toward April 1. In other words, you have submitted this list which, to me, seems in your letter a very powerful list, and I think what they will do is give a little bit but not the whole. And so the result will be unsatisfactory as far as we are concerned.

Let me ask you this. I am absolutely convinced that if you came up here with some rugged retaliatory legislation, going so far as saying there will be no admission of Japanese telecommunications equipment into the United States, absent them freeing up their markets to us, I think it would pass this Congress and reach the President's desk within 2 weeks. I think that is the attitude here. And the result of course would be that we wouldn't get their markets, but they wouldn't get ours—our manufacturers would get our markets, which would be a salutory one. Have you considered that? This is playing hard ball, I recognize that, but it seems to me this date you have set out of April 1 is a crucial one, and it greatly worries me. And it worries me to the extent that they will, as I said before, do marginal things but not the whole. Marginal would perhaps keep you happy, Mr. Olmer. And although I regret that you are leaving, because of that your anger threshold is probably higher than it normally would be. [Laughter.]

When are you leaving? Coincidental with April 1? [Laughter.]

Secretary OLMER. The lifting of the voluntary restraint, no, Senator. I plan to stay until June.

Senator CHAFEE. June?

Secretary OLMER. I like to think that I am open to all manner of possibilities, but I have not contemplated an exclusion of Japanese telecommunications products. I think that is the ultimate weapon.

Senator CHAFEE. It is draconian—no one would question that.

Secretary OLMER. It really is.

Senator CHAFEE. But what are we going to do?

Secretary OLMER. I suppose it is not enough for me to reiterate that the fact that the Prime Minister of Japan is the one who suggested to President Reagan—let's talk about elimination of all barriers in telecommunications. We have had this intense series of back-and-forth discussions, in which we have really tried to piece together the nuts and bolts of it because it is only through an understanding of the details that we figure out what it is we want them not to do. I just can't believe they won't take that message and implement it. I just know it is in their greater self-interest, not only in telecommunications, but in the interest of the larger relationship.

Senator CHAFEE. I know it, too, you and I both know it, and lots of other people may know it. By the way, when did Prime Minister Nakasone make this agreement with the President?

Secretary OLMER. On January 2 in Los Angeles when this new approach to trade negotiations between the two governments was first articulated, and it was his suggestion that telecommunications

be the No. 1 topic, and he made that recommendation, in my judgment, because he knew of this April 1 deadline.

Senator CHAFEE. Mr. Chairman, that concludes my time, but I think we should follow with Mr. Olmer and Ambassador Smith very closely this particular situation. It seems to me that this is a little different, as Mr. Olmer pointed out, than the normal situation. This isn't trying to rectify something that took place in the past. This isn't peeling back the onion. This is a major new critical date, and one that, if nothing happens or if it is a partial satisfaction, we ought to assemble again, Mr. Chairman, and see if we are not going to do something.

Senator DANFORTH. I agree, Senator Chafee, and we will have a Telecommunications Trade Act—we introduced that last year, and we will have another crack at that, which would, I think, directly deal with the subject.

Ambassador SMITH. Mr. Chairman, may I also indicate that what Lionel is talking about in terms of an April 1 deadline is only part of the overall sector problem that we are approaching. We are under the constraints of the April 1 deadline because of the legislative process in Japan, but after our hoped for success, we will go into a wider area in the telecommunications sector.

Secretary OLMER. Senator Chafee, I was asked whether or not it wouldn't be acceptable for the law and the ordinances and the ministerial guidance to take effect with some marginal change and then we continue working after April 1 to—the Japanese have indicated—we continue working after April 1 to maybe straighten out some other parts of it, and I would say that is not acceptable. I would say that they have got to do it before April 1. It is not acceptable to go through the process of passing it into law, of implementing the regulations, and of issuing instructions to the bureaucrats, and then have us come in, one by one by one, and say would you mind modifying this—that we need to do that before the 1st of April. So, the time window is very short, and your attention to it is deeply valued.

Senator CHAFEE. I want to say, Mr. Chairman, to Mr. Olmer I think his testimony was excellent, as was that of Ambassador Smith, in setting forth these specifics, on which you are obviously very knowledgeable. I am sure the Japanese will respond by saying we are bullying them, we are interfering in their domestic matters, in the telecommunications negotiations and all the standard answers that we would use here. But we are confronted with a very, very difficult problem for our manufacturers. I haven't objected to the automobiles coming in here or seeing our machine tool industry in Rhode Island suffer greatly because of these imports because, in many instances, they have had better products. But here is a case clearly where we have the better product, and we are not gaining admission, and that is wrong.

Senator DANFORTH. Senator Heinz.

Senator HEINZ. Mr. Chairman——

Ambassador SMITH. One point, if I may, Mr. Chairman. Whether or not this interferes in the domestic process of Japan, we have made it clear to the Japanese that while we are not pretending to get involved in their domestic processes they have international obligations, and that is what this is all about.

Senator DANFORTH. Senator Heinz.

Senator HEINZ. Mr. Chairman, thank you very much. Just listening to the discussion about what actions might be taken if by April 1 there was not sufficient performance by the Japanese Government, what kinds of retaliation—if that is the right word—are you thinking about if there is no performance that is satisfactory, and under what authority would you pursue it?

Secretary OLMER. I remember very well working with the chairman and his staff on his telecommunications bill a year ago, and I happen to believe that that is an excellent starting point, and I look forward to working with him again on it.

Senator HEINZ. Is that bill law yet?

Secretary OLMER. No. The administration did have some problems with it because in the view of many it would have been inconsistent with our own international obligations, but I think we believe that it could be fixed, and it could be made a useful instrument to achieve reciprocal access.

Senator HEINZ. So, as of April 1, you won't be able to take any strong action, even though you have said you want to take it.

Secretary OLMER. Not with that law. That won't be available by the 1st of April.

Senator HEINZ. That is all very well and good, but it seems to me once again we have repeated the old dance, which is on March 8, talk tough and set a deadline of April 1, and on April 1, continue to do very little. Do you want to answer that, Mr. Smith?

Ambassador SMITH. Senator, we are trying to give this effort a fair shake. As Lionel said he has been over there twice and we have had teams over there off and on for the last 4 months. We have set a deadline of April 1 for the Japanese and we must see what the reaction is by that time. Obviously, we also must consult with the American business community.

Senator HEINZ. Suppose you are no better off on April 1 than you are today?

Ambassador SMITH. Then, we as the negotiators, will take this to the Cabinet, with the continued understanding that we are not to prejudge this thing, if you will, until the day has arrived. We have set up in close coordination with the telecommunications industry of the United States a private sector team in Japan through the American Chamber of Commerce of Japan. We are in constant consultation with the industry as these ordinances come out.

After all, we depend on their advice to tell us whether these things that are being proposed by the Japanese are good, bad or indifferent. So, we as professionals are negotiating this, and if it is all a bust, we will certainly work through the Cabinet on April 1.

Senator HEINZ. You know one area where the Japanese have been talking to us for a long time is steel. The President, back in September, said that he would reduce steel imports, which were then running as high as 30 percent of the market, to 18.5 percent or less. At this point, the single largest shipper of steel to this country, Japan, has not signed off on an agreement. They, as I understand it, are the last major steel exporting country, besides being one of the biggest, not to reach agreement. Now, why shouldn't we just shut all Japanese steel out of this country if they

don't come forward on these negotiations? They certainly haven't been forthcoming on steel. How many chances do we give them?

Ambassador SMITH. Senator, I am not the steel negotiator. Ambassador Lighthizer is. I believe that most of the negotiation has been completed successfully. There are two or three issues, as I understood this morning, still outstanding, to which the two sides are continuing their negotiations on at this time, I believe.

Senator HEINZ. One last comment or question, I guess. In a sense, commendable as your negotiations are, it seems to me they still miss the whole point. We are being salamied time after time by the Japanese. We go and have a lengthy negotiation on telecommunications. It stretches out over a huge period of time—years—and we are sitting at the end saying we are going to determine just how tough we are going to be, even though we don't have any legislation to be tough with, by seeing how many little slivers of salami the Japanese give us on April 1, after having taken not only the salami and the bread and the lettuce and the tomatoes and everything else for the last 3 or 4 or 5 years. And then we threaten to do something—whatever that may be. And in category after category, they are slicing us neatly and thinly off like a piece of sashimi, which they so elegantly do, and our industries are being served up as the main course, with the result that everybody gets thrown out of work, after the Japanese get their little fork into us—or chopstick, as I suppose would complete the analogy properly. And they really do stick it to us at that. What is really the problem is not telecommunications or steel, automobiles or chocolate, or cigarettes, or magnetic resonating devices, nuclear resonating devices, and any 1 of 2 or 3 or 400 categories that you can name. The problem is the Japanese system, and you are not dealing with it. You are not getting to the core of the problem. I don't say this to be critical of you, Mr. Olmer, or of you, Mr. Smith, but what you have got are a bunch of sacred Japanese cows over there that say they don't want to go and drink. Now, it is easy for the cow to say it. It is very hard for you to lead the cow down to the water, and when you get to the water we don't even know if the cow is going to drink. [Laughter.]

So, maybe we ought to figure out exactly what it is that is involved here, you know, what is so sacred about this herd of cows? And we have got to change the religion. Otherwise, we are going to be doing this forever, and the trade balance is going to continue to be just like that wonderful chart that the Senate Finance Committee staff prepared; nobody is going to be exporting anything into Japan, and Japanese exports to others are going to continue to go off the map.

Secretary OLMER. I would like to make one comment. [Laughter.]

In respect of telecommunications, the heart of the problem is fairly simple to understand, and very difficult to do something about. And very difficult for the Japanese to undertake it. One always runs the risk of displaying empathy for the opposite side because it is oftentimes interpreted as agreement that nothing can be done. And nothing is further from the truth, but in the issue of telecommunications, they have a different language from us. When we use the term "privatization" and "liberalization" and "open market" and "free market," it doesn't mean the same thing. We

believe that we should limit the power of the FCC bureaucrat, and I don't use that in the critical sense at all. He should not be permitted to stop the introduction of cheap goods or of high technology goods which cost a lot. His only criteria is supposed to be will it harm the network? Now, I put that to my Japanese interlocuters just that way, and they said their perception of their responsibility to their people goes beyond that. They cannot accept the minimal role that we say is essential in a deregulated market and on April 1 they are supposed to deregulate. To us that means——

Senator HEINZ. Mr. Olmer, we are saying exactly the same thing. You have just done it more eloquently and more specifically. What are we going to do about it?

Secretary OLMER. I will leave that to the Deputy Trade negotiator. [Laughter.]

Senator HEINZ. Mr. Chairman, my time has expired.

Senator DANFORTH. Senator Matsunaga.

Senator MATSUNAGA. Thank you, Mr. Chairman, and in response to the question you put to me privately, the new ambassador from Japan is named Matsunaga. [Laughter.]

And just to keep the record straight, I am not he. [Laughter.]

Secretary Olmer and Ambassador Smith, in trying to reduce the balance-of-trade deficit, we need not only open up the markets for U.S. goods in Japan, but even reduce efforts on the part of Americans to import Japanese goods which compete with American products. I was very much disturbed by a statement made by Mr. Iacocca of Chrysler that he intended to import 300,000 units of small Japanese autos. Does your jurisdiction take you into discouraging businessmen such as this?

Secretary OLMER. In a deregulated market, Senator, no, sir, we have no authority to do anything at all about it, and I don't believe we would want to do anything about it if the authority existed. We wouldn't seek the authority.

Senator MATSUNAGA. So, even the manufacturers are complaining about unfair competition, on the one hand, and on the other hand, they themselves are promoting the import and the increase in deficits with Japan.

Secretary OLMER. I think the record should show clearly that much of Japan's success is not due merely to the hard work of its people and the enlightened policies of its government, but to American manufacturers who sold Japan technology for a generation which enabled them to make productivity improvements they wouldn't otherwise have been able to do for two generations or longer.

Senator MATSUNAGA. I just bought a new Chrysler and the salesman encouraged me to buy a specific type of Chrysler because it had a Mitsubishi engine. [Laughter.]

Sometimes we blame the Japanese when we should be blaming ourselves. I wish Senator Heinz would listen to this, but I see he has to leave. Now, on this chart, you indicate the U.S. merchandise trade balance with Japan. Does the term "merchandise" include agricultural products as well?

Ambassador SMITH. Yes, sir.

Senator MATSUNAGA. I see. Mr. Smith, you say you have been in the service since 1973, in a similar position?

Ambassador SMITH. I am a career foreign service officer, sir, on loan to USTR, and I have been involved in one form or another dealing with one trade issue or another since 1973.

Senator MATSUNAGA. I see. You have been asked questions about retaliation. I don't know whether this constitutes retaliation or not, but as you well know, having been to Japan 51 times, and as Secretary Olmer well knows the Japanese must have soybeans. They must have soy sauce and they have miso and tofu and aburagi and natto. If you take soybeans away from the Japanese, they would practically starve, as you well know. Do you recall in 1973 when the Japanese imposed a tax—I believe it was 15 percent of the sale of American securities in Japan—President Nixon at that time "retaliated" by invoking an embargo of all soybean exports to Japan. Japan at that time was importing 95 percent of all of its soybean leaves from the United States.

Would that be tantamount to retaliation?

Ambassador SMITH. Sir, one of the problems when one uses that word is the question of shooting oneself in one's foot. One of the results of that was, as you recall, the establishment of the soybean industry in Brazil.

Senator MATSUNAGA. That is right.

Ambassador SMITH. The effect was to the, if you will, detriment of the American agricultural soybean producer. So, when one talks about retaliation, one must be very careful that you are not using the word loosely.

Senator MATSUNAGA. That is the point I was about to make. What is the percentage of our soybean sale in Japan now? How many percent of the total import of soybeans do we export to Japan?

Ambassador SMITH. I don't know the precise figure, but somehow, sir, the number 65 percent strikes a bell, but I will get that and provide the accurate figure for the record.

Senator MATSUNAGA. I would appreciate that. This is an example of what retaliation can mean, and we have got to be awfully careful. Despite the fact that we have been suffering continued deficits in our balance of trade, haven't we actually increased sales to Japan over the years?

[The information for the record follows:]

U.S. SOYBEAN EXPORTS—CALENDAR YEAR 1984

	Million metric tons	Billion dollars
To the world	19.5	5.4
To Japan	4.14	1.2

Japan's soybean imports—calendar year 1984

[Million metric tons]

From the world	4.4
From the United States	4.1

Ambassador SMITH. We have increased sales to Japan, sir, but shall we say at a rate slower than they have increased sales to us,

so that the gap in the merchandise account is widening substantially.

Senator MATSUNAGA. A suggestion was made to me by the head of a very large Japanese firm, which has made investments here in the United States, that one of the problems with Americans investing and starting businesses in Japan is that they manufacture goods in Japan to export to the United States, which adds to the imbalance. He suggested to me that I suggest to people like yourselves—the Department of Commerce and the special trade representative—that you encourage the American businessman to manufacture goods for consumption by Japanese in Japan. What do you think?

Ambassador SMITH. Senator, I honestly think as a trade person that the less direction, guidance, or interference by a government into the market decisions or sourcing decisions of a firm, be it Japanese or American, the better. There are a number of U.S. companies who have manufacturing facilities in Japan and export the product—or import the product if you will—to the United States. We have nothing to object to, but we are saying—what our problem is—is that on items which are made in the United States, for example, or made by third countries who are also trying to get into the Japanese market, that the access opportunities are extremely limited and that Japan has an obligation, not just to the United States, but to the world as the second major economic power to act in that form; that is, to open its markets more.

Senator MATSUNAGA. But you would only be giving free advice. It would not be compulsory. I am suggesting sometimes a mere suggestion, and a mere suggestion which comes from those in business might help American business as well as to reduce our deficit balance of payments.

Ambassador SMITH. I think there are many in this country who would agee that Japan needs to do more to stimulate domestic demand.

Senator MATSUNAGA. What about the balance of investments—the United States in Japan as compared to Japan in the United States? Do you have that figure?

Ambassador SMITH. I believe that the investments in the two countries—and this may be a 1982 figure—is roughly in parity at about $8 billion each. I believe since 1982 there has been more Japanese investment in the United States than U.S. investment in Japan, but we will provide that for the record. What is surprising about that figure is that with the two powers being as large as they are that the investment is as small as it is.

Senator MATSUNAGA. I agree. But you will provide the figures for that?

Ambassador SMITH. We will provide the figures.

[The information submitted for the record follows:]

1983 foreign direct investment

[In billions of dollars]

United States in Japan	$8.059
Japan in United States	11.145

1982 foreign direct investment

[In billions of dollars]

United States in Japan	$6.928
Japan in United States	9.679

Senator MATSUNAGA. And investments are not at all included in the trade deficit figures?

Ambassador SMITH. No.

Senator MATSUNAGA. If I may continue on a local matter. Regarding chocolate candy, do you see any probability of Japan's acceptance of the proposal or in any way compromising by reducing the 20-percent rate to 7 percent or somewhere in between? Do you see any probability?

Ambassador SMITH. We have gotten them down from 35 percent to 20 percent. Hope springs eternal, and I have assured the interested parties that I am going to do my darnedest.

Senator MATSUNAGA. Hawaii is a great exporter of chocolate—the macadamia nut chocolates—to Japan, and chocolate manufacturers are disturbed that Japanese imports of chocolates amount to only 3 percent of the Japanese confectionery market.

Ambassador SMITH. That is correct, sir. And the U.S. confectionery industry has done a great deal to try to, if you will, counter the argument that they don't try hard enough. They do indeed try very hard, including labeling in Japanese. They have made a commendable effort, and they deserve our support.

Senator MATSUNAGA. I have received a number of inquiries from my constituents. We make what is known in Hawaii as pipikaula, like pastrami, dried beef, and the Japanese have placed real strict restrictions on the importation of that dried beef. Under what circumstances is the importation into Japan limited in this regard?

Ambassador SMITH. I was not aware of that particular beef product, that it was limited, sir. I spent an awful lot of time negotiating beef and citrus, but I was not aware of that. I will be glad to look into that.

Senator MATSUNAGA. Can you make an inquiry?

Ambassador SMITH. And I will report back to this committee.

[The information submitted for the record follows:]

ADDITIONAL INFORMATION REGARDING JAPANESE RESTRICTIONS ON PIPIKAOLA

Pipikaola is a Hawaiian product consisting of beef jerky soaked in soy sauce. Japan prohibits imports of products containing more than 70 parts per million of sodium nitrite or nitrate. It is likely that pipikaola exceeds this level due to the salt in soy sauce. In addition, Japan imposes a quota on prepared meats, which would include pipikaola. A 25 percent ad volorem duty is levied on this product classification also.

Senator MATSUNAGA. Then I can report to my constituents. Thank you, Mr. Chairman.

Senator DANFORTH. Gentlemen, you have been very patient. Let me just ask one other question on a specific subject. I understand that the United States and Japan have been negotiating for some time over new air routes between the two countries. I also understand that the United States is considering giving Nippon Cargo Airlines an air freight route in a freight market already dominated by Japan Airlines. Given the fact that NCA is 90 percent owned by Japanese freight forwarders and the six major Japanese steamship

companies that already monopolize the shipping lanes between the United States and Japan, what is the likely trade consequence of giving NCA this trade route? Have you studied the effects on bilateral trade of permitting NCA into the market and the effects of the probable leveraging that is positioned by its Japanese owners, and don't you think the trade consequences of this issue should be fully understood before the negotiations are concluded?

Ambassador SMITH. If I remember all the questions, sir, I think the answer is yes, but let me just say that this matter is being discussed at very high levels of the U.S. Government at the present time. We are looking at all the pluses and minuses of the whole issue, and our work is continuing in that area on a high priority basis. As you know, the President made a request to the ITC for a study of some of the elements to which you referred, sir. There have been discussions between the United States and Japanese aviation negotiators. The United States negotiators have reported back some of the results of their discussions.

Senator DANFORTH. Yes. I know there are discussions. I think the question is what are the trade consequences? It is one thing to have planes that are carrying tourists. It is quite another thing to have planes that are carrying cargo, particularly if there is a monopoly position established by Japan with respect to both air transportation of freight and ship transportation.

Ambassador SMITH. Senator, we are looking at that issue at this moment in conjunction with the Department of Transportation and other agencies of the Government. Literally, we are looking at this right now.

Senator DANFORTH. My understanding is that there already is a draft agreement, and my concern is that the State Department is barging ahead without any understanding of the trade consequences.

Ambassador SMITH. To my knowledge, sir, there is not an agreement in the normal sense that one uses that word. There have been discussions, and certain parameters have been talked about, but there is no agreement to my knowledge at this time.

Senator DANFORTH. All right.

Secretary OLMER. There will be no agreement and no administration position taken until all of the trade consequences are fully understood.

Senator DANFORTH. Good.

Secretary OLMER. In part, that is dependent on completion of the report by the International Trade Commission.

Senator DANFORTH. Gentlemen, I want to thank you. I think that it is one thing that deserves final comment, and that is the fact that here we are Friday—it is generally a day when Members of the Senate are returning back to their constituents. It is usually a very low attendance day for hearings, and yet we have had a very well attended hearing.

I think that this is indicative of the tremendous concern about the whole U.S. trade picture, particularly the situation with respect to Japan, but the whole U.S. trade picture, and a recognition of the fact—I think a growing recognition of the fact that the trade system just doesn't work—that it has clearly broken down, that this was not anticipated in 1947 when we entered into the General

Agreement on Tariffs and Trade, and that particularly a $37 billion trade deficit with Japan is just totally unacceptable, that it cannot be explained solely by the exchange rate problem, that even if we fix that problem somehow by budget deficit cuts or whatever, we would still have huge trade deficits with Japan. And it is just not right. I also think that there is a growing feeling, and it certainly is my belief, that negotiations have been valiantly undertaken but haven't really produced very much, and that they are not likely to.

The tendency of the Japanese is to negotiate and negotiate and negotiate and then negotiate some more. And the time has come really to do something, to take some action, and I think that that is what we are feeling our way toward. The voluntary restraint resolution that Senator Boren and I and 36 others introduced may not be the greatest idea in the world. Maybe we should come up with some other form of action to deal with this very serious problem. I don't think that it is going to be satisfactory to most of the people—not all, but to most of the people—here today if all we do is to shoot down everybody's idea, if all we do is to say, oh, no, we don't want to do that and we don't want to do this because we end up doing nothing. We end up doing nothing other than complaining, other than sending delegations over constantly—50 times, 15 times—to complain. That hasn't worked. I don't think it is going to work. I don't think there is any likelihood. These charts next year this time are going to look much worse than this, much worse for the United States and much worse for the rest of the world.

I want to make one specific suggestion. Maybe it is nonsense, but I think it is a good idea. If I am correct that Japan is a problem for the world, not just for the United States, it seems to me that what we should do is that our Government should confer with the rest of the world. We should set up some kind of meeting, some kind of conference—we like to go to meetings—with the United States and the Europeans and the LDC's and anybody else who is an aggrieved party and that the topic of the meeting is: What should we together do about Japan? I think we should do something. I think it is better to do something in concert with other countries than to do it ourselves, but that is just one suggestion. And I don't know if you have any particular response to it or not, but we begin a process of discussion toward a common policy adopted by the United States and the rest of the world to deal with and to redress the problem that we are having right now in the world with Japan. They are sucking the world dry, and it is not right, and we shouldn't put up with it. And we should act together to resolve the problem. I don't know if you have any comment on that.

Senator MATSUNAGA. Mr. Chairman, if I may comment on that. I think that you are suggesting that we never learned from history. If we forget history, we are doomed to repeat the mistakes of the past. What you are suggesting is what we tried to do before World War II.

Senator DANFORTH. History is on that chart.

Senator MATSUNAGA. Mr. Chairman, I would suggest that we look upon Japan as a trading partner and establish a condition such that they will look upon us as trading partners and not competitors. What we need to do as I can see it—and as was suggested

here earlier—is improve lines of communication, and learn more of each other's cultural differences for better understanding, Mr. Chairman. Do you have any Japanese-speaking negotiators?

Ambassador SMITH. Yes, sir.

Senator MATSUNAGA. You do.

Senator DANFORTH. I would suggest, Senator Matsunaga, that we have had incessant communications and that the Japanese look on us as trading patsies.

Senator MATSUNAGA. Comes April 1—and that April 1 date bothers me because I do hope the Japanese won't practice what we practice here on April 1. [Laughter.]

Senator DANFORTH. Would you like to respond to the question, or to the proposition?

Secretary OLMER. I know that several years ago a recommendation was made by the European Community that the United States join with it in a complaint in the GATT against Japan, and it was rejected at the time as a matter of U.S. policy because it was believed that it would tend to isolate Japan and that Japan was an important ally of the United States, in the words of Ambassador Mansfield and in the words of the President, perhaps our most important bilateral relationship in the world, a relationship that has component parts that transcend significant even in the numbers reflected in those charts. I think that the decision not to join with the EC on that complaint in the GATT was well taken and that it should be sustained. I understand your frustrations, Mr. Chairman, and I believe that it has come time to consider what will be done if we don't get deliverance on the objectives we have set for ourselves, but I share Senator Matsunaga's view, that is, Japan has just begun emerging as a participant in the world scene, reflecting its economic power and to, in a sense, tell it to go back and figure out what you need to do for yourself by yourself, if the rest of the world is against you, would have consequences, I believe, of a dire nature we would not want to confront.

Ambassador SMITH. Mr. Chairman, I fully share Lionel's view on that. I was one of those who wrote the paper which led to that decision. I am not 100 percent certain that I would want to align myself with the European Community as if they were the leaders of free trade in this world.

Senator DANFORTH. They are not the leaders of the free trade in the world, but if you look at that third chart, that shows the common problem that we have and the rest of the world. It seems to me that where there is a common problem, there should be common communication and a common strategy to deal with it.

Where we are heading now, Mike, is nowhere. Where we are heading now is absolutely nowhere, and where we are heading as a result of what we did when we extended the VRA's without any concessions by Japan on anything is to say to them: We are going to continue to complain, and we will continue to negotiate, but regardless of what you do—regardless of what you do to shut out our products, and there are many ways you can do it, and you will think of them all—and regardless of the size of the deficit and regardless of what you are doing to the rest of the world, our action will be simply verbal. And I think that that has failed, and I think that it will continue to fail as long as we do it. And those charts

are going to look like little charts, little figures compared to what we are going to see developing over the next 2 or 3 years. I really think that the administration should rethink its strategy. I think you are going nowhere.

Senator MATSUNAGA. Mr. Chairman, I think I have a little more faith in Mr. Smith and Mr. Olmer and the others who negotiate, and I will make this prediction that the chart will go the other way.

Senator DANFORTH. Gentlemen, thank you very much.

[Whereupon, at 1:12 p.m., the hearing was adjourned.]

[The following prepared statements were submitted for the record.]

Statement of Senator Packwood

Those who defend a free and open trading system must be increasingly disturbed over the difficulty of obtaining access to the Japanese market. I am among those defenders not only because the international trading system is founded on this premise, but because I believe our citizens and economy benefit greatly from the free interplay of competitive forces. But there are practical, as well as theoretical, limits to the growing inequity of our trading relationship with Japan. This inequity is reflective of a world-wide phenomenon in which Japan has become a relatively smaller importer of manufactured goods as it has accelerated its exportation of such goods. Even though Japan's economy has not grown as fast as our own during this past year, its growth is impressive relative to much of the world. Yet, its absorption of manufactured imports has hardly grown.

Whatever the complexities of Japan's endemic resistance to imports, there are some measures which could effectively and straight forwardly increase Japanese imports. One of these is the lowering of Japanese tariffs on wood product imports. Access to Japan's important market would greatly improve the prospects for the efficient and competitive American lumber industry and reduce the bilateral trade friction which threatens to undermine the alliance itself. I recognize that the Japanese government faces significant political resistance to the reduction of trade barriers, including the tariffs on imports of wood products. But, if our government is going to resist the equally strong pressures in the United States for protection and retaliation, the Japanese government must find the political will to do what must be done.

STATEMENT BY SENATOR MAX BAUCUS
INTERNATIONAL TRADE SUBCOMMITTEE
3/8/85
"JAPAN'S CLOSED MARKETS"

Introduction

America's Ambassador to Japan, Mike Mansfield, says that the relationship between the United States and Japan is "the most important bilateral relationship in the world."

He's absolutely right. The U.S. and Japan are the world's leading overseas trading partners. Our alliance is the foundation for peace and security in the Pacific Basin. And our citizens are bound together by close social and cultural ties.

Japan's Trade Barriers

But there's another side of the coin--a darker side. In 1984, we ran a $37 billion trade deficit with Japan. To put in another way, for every $1.00 worth of beef, timber, and wheat we sold to Japan, the Japanese sold $2.62 worth of cars, TVs, and VCRs to us. As a result, more than a million U.S. jobs shifted overseas.

This gross imbalance has many causes, including the high value of the dollar and the fast pace of our economic recovery. But one of the main causes is Japan's stubborn refusal to open up its markets.

One American wrote that he'd been unable to sell products to the Japanese because "they told us they had plenty of everything we had to offer."

That was in 1816. Since then, Japan has transformed itself from an isolated feudal kingdom into the free world's second-leading economic power, producing more steel, cars, and robots than any other country.

But some things haven't changed. Japan still protects its market as stubornly as in 1816. Sometimes, it's to protect inefficient but politically powerful groups, like the beef producers or the sawmill operators. Other times, it's to incubate "sunrise" industries like telecommunications and satellites until they can compete on their own.

In either case, Japan's protectionist policies have a devastating impact. First and foremost, they deny American companies about $10 billion a year in direct sales.

What's more, Japan's protectionist policies force other Asian countries to flood the U.S. with cheap imports. These countries

can't crack the Japanese market. But they need foreign exchange. So they divert their products from Japan, which buys only 8% of Third World exports, to the U.S., which buys over 50%.

Finally, Japan's protectionist policies undermine public confidence in the open trading system. People aren't stupid. They can see that Japan wants free trade when it has a comparative advantage, and protectionism when we do. As a result, many Americans are beginning to question whether the postwar trading system makes sense anymore.

America's Response

Up until now, America has responded to Japanese protectionism meekly. We've tried to achieve free trade by example. And we've tried to resolve disputes through endless rounds of painstaking negotiations. These negotiations have, by and large, failed. Sure, some barriers have been reduced. But new barriers have replaced old, so that U.S. sales have not substantially risen.

Visiting Japan a few weeks ago, I learned about this process first-hand. I asked a Japanese industrialist whether the pending privatization of Japan's giant telephone company, NTT, would result in higher U.S. sales. He replied that it probably would not. There were so many Japanese suppliers already, he said, that it was like a hotel where "the doors are open, but the rooms are full."

New Tactics

When I heard this, I remembered an old Japanese proverb. It says, "The sack of a man's patience is tied with a slip knot."

Well, my patience is running out. Each time we confront Japan's stubborn refusal to open its markets wider to U.S. products, I become more convinced of what an American businessman wrote me last year. During the negotiations over Japan's beef quota, I held a press conference for Japanese reporters, to announce that I was linking my vote on the domestic content legislation to the successful resolution of the beef negotiations. A short time later, I got a letter from an American businessman living in Tokyo who had seen my picture in the Japan Times. During his 11 years in Japan, he said, he had "concluded that the Japanese understand only one thing when it comes to international negotiations: Matter-of-fact power.... They will not accept the seriousness of the situation and the resolve of the U.S. and other countries until concrete measures have been implemented to force reciprocity."

So what should we do?

Last year's trade bill gives the President broad authority to retaliate against unjustifiable foreign trade practices. If the current sectoral negotiations don't result in substantial Japanese

concessions, President Reagan should retaliate. And if he won't, we will.

Specifically, we should consider:

--selectively denying Japan access to our trillion-dollar market;

--negotiating bilateral agreements that give preferential treatment to Japan's neighbors if they will agree to trade fairly;

--imposing a stiff import surcharge on Japanese products;

Conclusion

Mr. Chairman, I'm reaching this conclusion very reluctantly. Like most other members of this Committee, I support the open trading system. I believe that everybody's better off when goods and services flow freely and trade keeps expanding.

But we must send Japan a message.

After World War II, it may have been appropriate for Japan to become a kind of "Asian Switzerland," concentrating on economic development and avoiding involvement in international affairs.

But modern Japan is not Switzerland. Japan is the free-world's second-leading economic power. It should begin to play a political role equal to its economic role. As Robert Samuelson wrote earlier this week, "Japan is a great nation. It must start acting like one." In other words, Japan must assume a greater role maintaining public support for the open trading system.

This means more than calling for another round of GATT negotiations. Japan must lead, and make some of the sacrifices leadership demands. Japan's own "Federation of Economic Organizations" put it well: "At this critical juncture Japan must proceed in opening its markets in a thorough manner." Let me be more specific. Japan should open its markets to U.S. forest products; to telecommunications equipment; to electronics; and to pharmeceuticals and medical equipment.

Otherwise, there will be a trade war. And Japan has a lot more to lose than we do.

STATEMENT BY

SENATOR CARL LEVIN (D-MICHIGAN)

ON S. CON. RES. 15 ON JAPANESE TRADE

MARCH 8, 1985

I would like to thank the committee for giving me this opportunity to submit testimony on Senate Concurrent Resolution 15. I am pleased to co-sponsor this resolution, and I urge the subcommittee to report it favorably. The Resolution, proposed by Chairman Danforth and Senator Boren, is now cosponsored by 36 other Senators. This resolution urges: "That the voluntary restraint on Japanese autos not be ended until United States exports to Japan are substantially increased and the United States trade deficit with Japan is substantially reduced."

The resolution would inform the President that he has made a serious negotiating mistake. In announcing that the Administration was going to lay down its defenses against Japanese automobiles, the Administration was in effect telling the Japanese: "Do what you want to our automobile industry...."

Mr. Chairman, I find such capitulation unacceptable. As William Safire wrote recently: "It's as if the unilateral disarmers have taken over at the White House, urging us to turn in our economic bargaining chips...." I agree with Mr. Safire. Why does President Reagan think that he can negotiate with the Japanese from a position of weakness?

The current voluntary restraint agreement (VRA) expires on March 31, 1985. Retaining those restraints is extremely important not only to the American auto industry but also to other sectors of our economy

which are struggling to improve their international competitiveness. By allowing the VRA to expire, the President could be responsible for reversing the slow decrease in the unemployment rate that we have been experiencing over the past two years.

The most serious harm from ending the VRA will come from increased import penetration by Japanese automobiles. In 1984, Japanese imports constituted 18.3 percent of U.S. car sales. If the VRA is dropped, Japanese control would increase to 21.3 percent in 1985, to 25.2 percent in 1986, and to 27.7 percent in 1987, according to a recent Commerce Department study. The study also notes that a price reduction in Japanese cars, spurred by a "price war," could increase Japanese penetration even further. While I find these projections troubling enough, I have a suspicion that the numbers might be unrealistically low. There are several smaller Japarese automakers, such as Suzuki, Mitsubishi, Isuzu, and Daihatsu, which would surely love to capture a share of the U.S. market, and might go to extraordinary lengths to do so. I have seen estimates ranging as high as 4 million for the total number of cars that Japan could ship to the U.S. The increase to 27.7 percent of the U.S. market by 1987 represents about 3 million vehicles a year. At 4 million vehicles, Japan would capture 37.7 percent of the U.S. market.

When Japanese imports increase, American workers lose their jobs. The job losses occur not only among auto workers, but also among other workers in the steel, rubber, glass, iron ore, textiles, machine tool, paint, aluminum, and copper industries, plus workers in disparate supplier and service industries. Every automobile job supports about 2.3 jobs in other industries. The Commerce study I

mentioned above estimated that by the end of 1987, the employment loss would be 125,000. A study by the United Auto Workers estimates a much higher loss of 200,000 jobs by the end of 1986.

In addition to these job losses being extremely costly to the workers and families directly affected, they are also costly to all of us in an indirect way. Idle workers and plants mean less tax income to the federal treasury and more government spending in the form of unemployment insurance, food stamps, medicaid and similar programs. Forcing the layoff of thousands of workers worsens the already horrendous problem of the federal deficit.

The second economic blow from dropping the VRA would come from U.S. automakers shifting abroad their production and investment in autos. If the U.S. dismantles all its defenses against imported cars, we would be adopting a trade policy radically different from virtually every other industrialized country in the world. There is no such thing in real life as textbook free trade in automobiles. For example, while the U.S. imports about 23 percent of its automobiles, European countries import about 7 percent.

So what will happen when the Reagan Administration sacrifices the VRA on the altar of free trade? The American automakers, being profit seekers, will find it in their interest to transfer more and more of their production abroad. And, as such overseas transfers occur, more domestic workers will lose their jobs.

The third wound from tearing up the restraint agreement will be a likely decline in Japanese investment in automobile production in the U.S. When Honda, Nissan, Toyota, and Mazda decided to set up plants in the U.S., they were making a political judgment that if they

wanted to sell cars to American consumers, then they'd better start producing some of the cars here. The recent Commerce Department study estimates that sales of U.S.-built Japanese cars will increase from 133,000 vehicles in 1984 to 675,000 in 1987. But I ask you, if there is to be no VRA, no significant automobile tariff, and no domestic content legislation, then why should Japan bother? The Japanese are very practical businessmen. Will they continue efforts to produce 675,000 cars here if they don't have to and they can produce them more cheaply in their home plants? I doubt it.

In the past year or so, the VRA has finally begun to work. The American auto industry is finally recovering. To abandon the VRA now on the grounds that the auto industry, after several disastrous years is finally earning profits again, would be an incredibly myopic decision. There is just too much at stake in terms of American jobs and in terms of the economic health of many of our states and communities for us to permit Japan to ravage our markets.

Senate Concurrent Resolution 15 properly draws the attention of the Senate, the nation and, I fervently hope, the Japanese to the fact that our openness to Japanese automobiles ought to be linked to the other bilateral trade issues with Japan.

Japan has probably the most unfair trading practices of any coauntry in the world, and it's time we did something about it. Out of our 1984 trade deficit of $123 billion, almost $37 billion, or 30 percent, comes from the U.S. deficit with Japan. Our trade with Japan, by and large, is only a one-way street. Japan sells to us, but won't buy much from us.

The horror stories of trying to do business with THE JAPANESE are well known to my colleagues. Beef, forest products, citrus, wheat, rice, tobacco, wine, photographic paper, aluminum, advanced medical technology, pharmaceutical products, telecommunications, and high electronics -- you name it and Japan has a high tariff, a low quota, a testing requirement, a currency control, a government regulation, or some other excuse for not buying from the U.S.A. They don't even let American lawyers set up offices in Japan to represent American companies trying to cut through the thicket of trade barriers.

I am aware that there are ongoing trade negotiations with Japan, but most of the reports I have received are not encouraging. Their proven actions over a long period of time do not live up to the rhetoric of the incoming Japanese Ambassador to the United States, who recently stated, "We owe to the United States our present prosperity. I believe it is our responsibility to open up more of our domestic market to foreign products."

The Reagan Administration must follow up on remarks like these, and do a much better job of convincing the Japanese to allow American companies access to Japanese markets. The Administration must be tough, and must display a willingness to penalize the Japanese if they do not trade fairly. Far from dismantling the VRA, we should be adding to our economic artillery to increase the chance of penetrating their bubble of intransigence.

This resolution should go further in one important respect. The Administration should find a way to encourage other auto producing nations to lower their restrictions on cars from Japan. For example, France restricts Japanese imports to about 3% of its market. Italy limits Japanese imports to only 2,200 cars a year. Allowing our restraints to lapse while restraints imposed by other countries continue to exist will result in Japanese auto producers focusing on increasing even further their U.S. market share to our great detriment.

Again, I thank the Chairman for the opportunity to present this statement before the Committee.

Chocolate Manufacturers Association

OF THE UNITED STATES OF AMERICA

7900 WESTPARK DRIVE SUITE 514 McLEAN VIRGINIA 22102 • (703) 790-5011
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Mr. Chairman, Members of the Committee, I am Richard O'Connell, President of the Chocolate Manufacturers Association of the U.S. A. (CMA) and the National Confectioners Association (NCA). The two associations represent 110 chocolate and sugar/confectionery companies with 160 facilities in 31 states.

The industry, which employs around 55,000 people, is a major user of three agriculture commodities - sugar, peanuts, milk and milk products.

In nineteen-hundred-eighty-three, sugar ingredient consumption was 1.5 billion pounds; peanut consumption was 338 million pounds and milk and milk product use totaled $430 million.

The wholesale value for 1983 industry sales was $6.5 billion.

Today I wish to comment on a particular aspect of Japanese-American trade, and that is trade between the two countries involving chocolate confectionery.

# # # # #

The Chocolate Manufacturers Association of the United States and the fifteen companies it represents has requested that Japan act decisively to eliminate tariff barriers to imported chocolate confectionery (Schedule no. 18.06.100). Japan's action in 1982 to reduce the tariff on these items from 31.9% ad valorem to 20% ad valorem was a welcome step, but it went only part of the way in removing the major obstacle to U.S. exports.

As the principal supplier of chocolate and chocolate confectionery to Japan, we ask that Japan achieve parity with the U.S. duty rate of 7% by 1986, with an interim, transitional rate of 10% ad valorem to become effective in April, 1985.

The confectionery industries in Japan and the United States are of equal stature in the business of successfully manufacturing chocolate and chocolate confections of outstanding quality and consumer appeal. They are both mature, diverse industries composed of companies ranging from multinational corporations to small family enterprises. They share a like minded devotion to imaginative product development; an insistence on quality materials that assure consumer satisfaction and well-being; and an awareness of the importance of value received for money spent.

As businessmen, they also share manufacturing environments with similar constraints. Both American and Japanese confectionery companies confront elevated raw material costs that are a function of their nations' domestic agricultural price support programs including sugar, dairy, and peanuts. Using sugar as an illustration, an American confectionery company buying No. 11 raw sugar futures for October delivery will have to pay an additional cost of 17.75 cents per pound over today's world price of 4 cents per pound and the U.S. price they will pay for October deliveries of 21.75 cents per pound. Many Japanese companies have similar purchasing requirements.

Japanese confectionery companies, like their American counterparts, are increasingly turning their attention to exports. Japan's exports of chocolate confectionery, while still modest, more than doubled between 1980 and 1983 growing from 646 metric tons to 1,468 metric tons. Exports of chocolate from Japan to the U.S. have also increased dramatically from 4 mt in 1980 to over 85 mt in 1983. The U.S. industry too is putting more emphasis on exports, particularly to the Far East. There is a renewed effort to reduce tariff and nontariff barriers to confectionery exports to Taiwan and South Korea as well as expand sales in Japan.

Amidst a host of similarities, there is one outstanding difference. The U.S. industry competes and succeeds in a free an open domestic marketplace. The challenge of competitive imports is accepted. The industry has not looked to tariff and nontariff barriers for protection. U.S. tariffs, at 5% for solid chocolate and 7% for chocolate and sugar confectionery, are among the lowest in the world. Further, the U.S. has not used high tariffs to compensate or subsidize confectionery companies for the increased costs that result from agricultural price support programs governing their essential raw materials.

The circumstance in Japan is quite different. Five conglomerate corporations, Meiji, Glico, Lotte, Morinaga, and Fujiya control 86% of a chocolate confectionery market valued today in excess of Yen 397 billion. Despite their strength and maturity, they are protected by a 20% ad valorem tariff that is among the highest of any industrialized nation. The U.S. rate is 7%, the EEC average is 15%, and Canada, 12.5%.

Japan's 20% ad valorem tariff on chocolate confectionery, which became effective in April, 1983, was lowered from previous levels of 35% in 1979, 33.1% in 1981, and 31.9% in 1982. In the past, Japan has attempted to justify maintaining such high tariffs on the grounds of protection for infant industry, and compensation for high raw material costs resulting from agricultural price support programs. The financial depth and product sophistication of Japan's confectionery companies contradict the first rationale. The second circumstance is common to confectionery manufacturers in the U.S. and Europe and yet almost all these nations maintain tariffs well below Japan.

It is time for Japan's confectionery industry to accept the stature it has earned and the responsibility of supporting Japan's leadership toward freer world trade. Japan must set the example and the pace for dismantling trade barriers in Asia and increasingly in the entire free world. Meiji, Glico, Lotte, Morinaga, and Fujiya should do no less than participate in the fulfillment of Japan's new economic statesmanship.

Appended to this statement and also submitted for the record of these hearings is the request sent to Prime Minister Nakasone of Japan by Members of the Senate requesting that the tariff be reduced to the U.S. rate of 7%.

RICHARD G. LUGAR
INDIANA

SH 306 SENATE OFFICE BUILDING
WASHINGTON D.C. 20510
202-224-4814

COMMITTEES
FOREIGN RELATIONS
AGRICULTURE NUTRITION AND FORESTRY
SELECT COMMITTEE ON INTELLIGENCE

United States Senate

WASHINGTON, D.C. 20510

December 13, 1984

His Excellency Yasuhiro Nakasone
Prime Minister
2-1 Kasumigaseki
1-Chome, Chiyoda-ku
Tokyo 100, Japan

Dear Mr. Prime Minister:

The Government of Japan has frequently called upon American industries and workers to accept import competition as a constructive force in the marketplace. Today the U.S. confronts a $32 billion trade deficit with Japan and the resistance by many Japanese industries to accepting American exports on these same positive terms. Significant progress could be achieved toward our mutual goal of correcting this imbalance if decisive tariff reductions are made in 1985 for U.S. exports that have demonstrated sound competitiveness in Japan's market.

Chocolate confectionery is among these products and the U.S. industry considers Japan an especially important market. The increased purchasing power and interest in Western products among Japan's consumers and the strength and sophistication of your domestic confectionery manufacturers should result in healthy competition that will benefit Japan as well as the United States.

Japan's consistently high tariff on chocolate confectionery has thus far discouraged competition. Japan's ten largest confectionery companies produce most of the chocolate consumed domestically and the top five control 86% of the total market. Imports have been limited to a 3% market share.

Despite high import tariffs, Japan's confectionery companies have been unsuccessful at increasing domestic demand for chocolate confectionery. Historical evidence suggests that when American chocolate confectionery establishes itself in a foreign market, the market itself expands for both domestic and foreign manufacturers.

An industry with a 97% share of its domestic market and the ability to more than double exports of chocolate confectionery in three years should not require a level of tariff protection that is among the highest of any industrialized nation. Neither can a lowering of the tariff be rationalized as potentially damaging to Japan's sugar and dairy industries. Chocolate confectionery production consumes only 2% of Japan's total demand for refined sugar and 2.4% of its total demand for dry milk.

U.S. exporters are efficient, competitive producers anxious to contribute to the expansion of Japan's market. They have sustained their position among otherwise declining imports by custom packaging and more effective advertising. They find, however, that their goal of improving price competitiveness and market expansion is being undermined by the 20% tariff.

The United States Trade Representative has called upon Japan to reduce its tariff on chocolate confectionery from 20% to the current U.S. rate of 7% by 1986, with an interim rate of 10% in 1985. We support this proposal and look for it to be the first step toward achieving a more equitable balance of trade between our nations.

Sincerely,

John Glenn

Richard G. Lugar

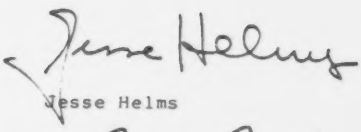
James Abdnor

Bill Bradley

Dennis DeConcini

John Heinz

Daniel Inouye



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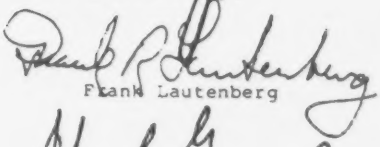

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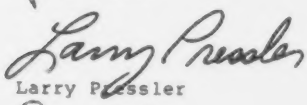
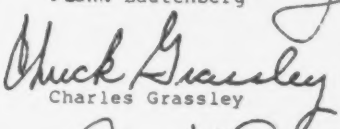


Larry Pressler



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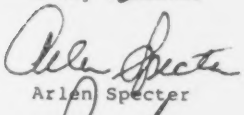

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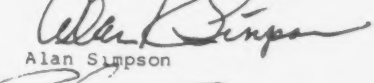

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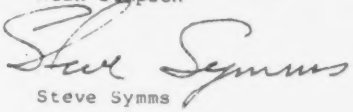

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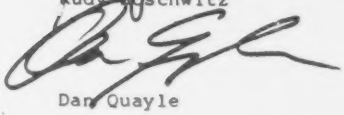

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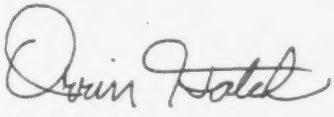

Orrin Hatch

STATEMENT

of

the

AMERICAN ASSOCIATION OF EXPORTERS AND IMPORTERS

ON THE

UNITED STATES - JAPAN TRADE RESOLUTION ISSUE

before the

COMMITTEE ON FINANCE
SUBCOMMITTEE ON INTERNATIONAL TRADE

of the

UNITED STATES SENATE

March 8, 1985

On March 1, 1985, President Reagan decided to leave the decision of whether to extend the voluntary restraint agreement on Japanese autos (VRA) to the Japanese. Nonetheless, protectionist feeling remains strong in Congress and there have been numerous calls to renew the VRA with Japan, even though the U.S. auto industry is enjoying record profits. The American Association of Exporters and Importers believes that any attempt to extend the VRA, in spite of President Reagan's decision, is to protect a healthy and increasingly profitable industry at the expense of the American consumer. Protection of a healthy domestic industry is a dangerous precedent that will lead to the contraction of world trade.

The American Association of Exporters and Importers is a national organization comprised of approximately 1100 U.S. firms involved in every facet of international trade. Our members are active in importing and exporting a broad range of products including chemicals, machinery, electronics, textiles and apparel, footwear, foodstuffs, automobiles and wines. Association members are also involved in the service industries which serve the trade community such as customs brokers, freight forwarders, banks, attorneys and insurance carriers.

The American Association of Exporters and Importers shares the concern of the Subcommittee and the general public regarding the increasing trade and budget deficits. We do believe that the value of the dollar should reach a level where U.S. exporting firms are not penalized in foreign markets and can compete on the same footing as other suppliers from other countries.

To this extent the budget deficit must be reduced to prevent interest rates from increasing. High interest rates further spur demand for the dollar making it more attractive to investors and appreciating its value vis-a-vis other

currencies. The higher the value of the dollar, the harder it is for U.S. exporting firms to compete in foreign markets. However, trade restricting actions are not the answer to problems caused by the misalignment of currencies.

AAEI agrees with Senator Danforth that increased foreign market access will expand world trade to the benefit of U.S. exporting firms and help to reduce the trade deficit. We believe, however, that any proposed measures to increase access to foreign markets must be in accordance with our international obligations, and must be measures that will not "shoot our own foot."

The Resolution sponsored by Senators Danforth and Boren, and by Representative Michel calls for the extension of the VRA with Japan until "United States exports to Japan are substantially increased and the United States trade deficit with Japan is substantially reduced." These unquantifiable goals are only a small part of the problem with this resolution.

Using the VRA as a "club" to force Japan to open its markets wider to U.S. business is wrong for a number of reasons. First, using the VRA in such a way may lead to retaliation, thus having the undesirable effect of further hampering U.S. exports. Second, attempting to use the VRA as a bargaining chip is futile. The President has already announced his intention to allow the VRA to expire at the end of this month, on March 31. Any Congressional attempt to extend the VRA would serve only to continue to burden the U.S. consumer. To gain negotiating leverage, one country must threaten to take action or refrain from taking action that will penalize its trading partner. The threatening country, in theory, will

then be able to gain concessions, in this case, trade concessions from the threatened country. However, if Congress decides that the VRA should be continued, Japan and its auto industry will not be penalized. The Government of Japan, through its Ministry of International Trade and Industry (MITI), which is empowered to regulate the VRA, is enjoying more control over their domestic auto industry. Further, the Japanese auto industry, according to Robert Crandall of the Brookings Institution, made at least $2 billion per year of income, over and above what they would have made if the quotas had not been in place. Japan, and at least its large producers of cars, have little to lose if the VRA were extended.

This attempt to force Japan to grant greater access to its markets to the United States will penalize only one entity: The U.S. consumer. In the past four years the VRA has already cost the U.S. consumer billions of dollars and has had a negligible effect on employment. In fact, the FTC has estimated a cost to the U.S. consumer of $240,000 per job saved. What has resulted over the past four years is a massive subsidy to the U.S. auto industry, underwritten by the U.S. consumer.

AAEI is certain that the U.S. consumer will not and does not enjoy subsidizing a healthy U.S. industry so that Congress can toss empty threats at our trading partners. It is obvious that using the VRA as leverage to reduce our trade deficit with Japan will not work. The trade deficit can be reduced, not by bullying tactics, but by positive negotiation and by taking steps to bring down the value of the dollar, thus allowing U.S. exporters an even greater opportunity to penetrate foreign markets.